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MANAGEMENT REVIEW

DECEMBER 1961

PROTECTING YOUR CORPORATE TRADEMARKS

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The Pros and Cons of Executive Stock Options

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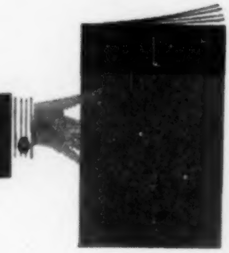

- **Something of Value.** As more companies introduce new products, expand into new fields, and distribute their products nationally and in foreign markets, trademarks have become increasingly valuable properties, and it has become more important than ever for management to take the steps necessary to protect them. This month's opening feature discusses how companies can handle and police this important area to insure against infringement, litigation, or the serious competitive damage that can result from the loss of a valuable trademark.

- **Service with a Sell.** Customer service is more than a necessary evil—it has proved to be a prime source of sales volume and profit. On page 34, Richard W. Harbison points out some of the reasons and relates the experiences of such leading companies as the Worthington Corporation, Singer Sewing Machine Company, Addressograph-Multigraph, and Modine Manufacturing Company.

- **Stock Options—Pro and Con.** Increasingly broad use of stock options as a form of management compensation has provoked some sharp reactions in the business community. In his article on page 47, Richard C. Smyth discusses the major criticisms of stock-option plans and their unique advantages to companies using them.

- **1961 Index.** This issue contains the index to Volume 50 of Management Review—January-December, 1961.

— The Editors

DECEMBER 1961
VOLUME 50, NO. 12

MANAGEMENT REVIEW

SPECIAL FEATURES

BUSINESS DIGESTS OF THE MONTH

THE MONTH'S BEST IN BUSINESS READING

DEPARTMENTS

COVER ART BY PAGEANT STUDIO

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Protecting Your Corporate Trademarks

■ Tom Mahoney

THERE'S A BOOM in trademarks today—a boom that grows constantly greater as more companies introduce new products, expand into new fields, modernize old trademarks, and distribute their products more widely, both nationally and in foreign markets. Approximately half a million trademarks are already on file at the United States Patent Office, and more than 20,000 new applications are being filed every year. In this welter of names and symbols clamoring for recognition in the market place, well-established trademarks, always major business assets, have become more valuable than ever—and it has become more important than ever for companies to take the steps necessary to protect them.

The danger is not only infringement, although the statistics indicate that this is a real enough problem: In 1960 alone, according to *The Trademark Reporter,* leading journal in the field, the courts decided 845 cases on trademark issues. More

A MANAGEMENT REVIEW SPECIAL FEATURE

dangerous, however, is the possibility of losing a trademark by default. If, for example, a mark is not used properly and consistently, it is seriously jeopardized. If a competitor is allowed to use a similar mark without challenge, the right to its exclusive use may be lost. And even when a mark is well known and securely established, improper usage may put it in the public domain by permitting it to degenerate into a generic name for the article on which it is used—as witness the fate of aspirin and cellophane. In fact, it is generally true that the more successful a trademark becomes, the greater is the need to protect it.

Who Steals My Purse . . .

Although they are commonly valued at a dollar on corporate balance sheets, trademarks can obviously have great value. A company that has earned a reputation for the quality and integrity of its trademarked products and has made a substantial investment in advertising them may well find its trademarks to be worth millions of dollars. The courts have recognized this fact, and sizable sums are often involved in trademark litigation; the National Lead Company, for example, was awarded $239,000 in 1959 when another firm's mark was found to infringe on the well-known Dutch Boy trademark. Twenty years ago, a justice of our highest court confirmed the value of trademarks:

> If it is true that we live by symbols, it is no less true that we purchase goods by them. A trademark is a merchandising shortcut which induces a purchaser to select what he wants, or what he has been led to believe he wants. The owner of a mark exploits this human propensity by making every effort to impregnate the atmosphere of the market with the drawing power of a congenial symbol. Whatever the means employed, the aim is the same—to convey through the mark, in the minds of potential customers, the desirability of the commodity upon which it appears. Once this is attained, the trademark owner has something of value.

If they are potentially so valuable, then, it follows that a company planning a venture that will result in a marketable product or service should devote the time and effort necessary to select the best possible trademark—and to protect it from loss.

What's in a Name?

A good trademark performs three important functions:

1. It distinguishes the product from those of competitors.

Tom Mahoney is the author of several books on business subjects, including *The Great Merchants, The Merchants of Life,* and *The Story of George Romney*. Mr. Mahoney wishes to thank The United States Trademark Association for permitting him to draw on facts presented in their comprehensive volume, *Trademark Management: A Guide for Businessmen* (New York: The United States Trademark Association, 6 East 45 Street, New York 17, N.Y., 130 pages, $3.00).

2. It serves as a guarantee of consistency of quality.

3. It helps to advertise and sell the product.

Let us assume that you are selecting a trademark for a new product that your company is about to put on the market. This is a project that takes time, ingenuity, and hard work—and it is not a do-it-yourself job. It requires the advice and assistance of specialists: trademark counsel, to report on legal aspects, as well as specialists from public relations, sales, design, advertising, and other areas of the company that will be affected.

In view of the hundreds of thousands of trademarks already registered and in use, it is obvious that some ingenuity will be required to settle on a name that will be distinctive and attractive without infringing on existing marks. To start with, then, you might consider the advisability of using a "house mark" or an already established "special product mark" of your firm.

House Marks

There are decided advantages to identifying a new product with a well-known house mark like Du Pont, General Electric, or Heinz. When the public image of a company is already favorable and its name is widely known, the selling job for a new product is obviously easier; moreover, advertising and promotion of any product bearing the house mark benefits all other products in the line, some of which may not justify the expense of separate advertising. Some companies, however, are reluctant to use their house mark on a new product until it has proved itself, to avoid the risk of incurring ill will for their entire line.

Special Product Marks

A "special product mark" already being used on a specific product may also be extended to cover the new product. Listerine, for example, began as a trademark for an antiseptic and was later extended to toothpaste and mouthwash. There are many cases, of course, where such an extension would not be feasible. A brand name that is definitely associated with a specific product might be inappropriate for another product or for a product in another area. Vaseline, long associated with petroleum products, might be considered unsuited for a product intended for consumption, and Swing-A-Way, used on hinged wall can openers, would probably be inappropriate on a product that was not designed to "swing away." On the other hand, Frigidaire was successfully extended from refrigerators to stoves, and Hotpoint from stoves to refrigerators, so such applications are not without precedent.

Sometimes a derivative of an existing trademark can be used to good advantage. Eastman has done this by adopting such marks as Kodachrome, Kodacolor, and Koda-

scope—based, of course, on the highly successful Kodak mark.

A New Trademark

When, for one reason or another, your existing marks will not answer your purpose, you will be searching for a new one. Generally speaking, it will probably fall in one of these categories:

1. An invented or coined word. Examples of such trademarks include Sanka, Koroseal, Kleenex, Jeep, and Spam.

2. A word that is suggestive (*not* descriptive) of the article. A good example is American Cyanamid's Formica mark, which suggests the molded parts to which it is applied. Similarly, Fiberglas is effective for a form of glass and Bufferin for buffered aspirin.

3. A business or family name, or a derivative of such a name. Bayer, Squibb, Ford, Chevrolet, Schlitz, and Studebaker are examples of this group. Kelvinator is derived from Lord Kelvin, the scientist who pioneered thermal research. The late King Fuad I of Egypt is memorialized by Fuadin, a drug trademark.

4. A portrait, picture, symbol, or other illustration, which may be accompanied by a word or phrase. One of the best-known picture trademarks is the red S of The Singer Manufacturing Company. The girl in it is modernized every few years to take note of changing styles in hair and clothing. White Rock's Psyche became a trademark when executives of the mineral water company saw Paul Thumann's painting of her at the Chicago World's Fair in 1893. Successful animal trademarks include Elsie the Cow, the terrier of "His Master's Voice," Leo, the MGM lion, and the Camel of cigarette fame.

More Than Meets the Eye

At first blush, selecting an attractive and appropriate trademark might not seem to present many problems, but the deeper one gets into it the more stumbling blocks appear. The very fact that last year almost one out of every five applications for new trademarks was rejected by the Patent Office indicates that there is more to trademark selection than meets the eye. Even after the selection team has thrashed out such knotty problems as finding a name that is easy to remember, read, and speak, a name that has no undesirable connotations, one that lends itself to pictorialization and is adaptable to any advertising medium, one that is suitable for foreign markets if the product will be sold overseas, and one that has the intangible imaginative element that makes it stand out from the ordinary—even then, many legal requirements remain to be considered.

For one thing, the mark selected usually cannot resemble another already in use. Eagle is a trademark for both pencils and condensed milk,

but the name Minute Maid for frozen steaks was recently ruled too similar to the Minute Maid trademark already used for frozen orange juice. Patent Office tribunals have ruled against many marks when they found that a likelihood of confusion existed between the proposed mark and a trademark already used on a similar or related product.

Less obvious, perhaps, is the fact that a trademark may be suggestive of the product on which it is used, but it cannot be descriptive. Talon for slide fasteners, Halo for shampoo, Mallard for raincoats—such marks suggest the qualities of the product without describing it; but "Extra Dry" is too descriptive to be registered as a trademark for wine, as is "Retractable Anvil" for a stapler with a retractable anvil. Similarly, geographical names are free to all whose business is located in an area, and family names may be used by all who bear that surname. Exceptions to these exclusions will be made only if it can be shown that, through long and substantially exclusive use, the name has come to identify and distinguish the product of a specific manufacturer—in other words, that a secondary meaning has been established.

There are, in addition, other prohibitions, the rationale of which

MARK OF THE MAKER

TRADEMARKS ARE NO NEWCOMERS on the business scene; they date from ancient Egypt and Greece, and pottery 4000 years old marked with the emblem of the maker has been dug up in the ruins of Corinth. In the Middle Ages, goldsmiths and silversmiths were required to mark their wares for the protection of the public. In England, the marks were filed at Goldsmiths' Hall, and some of these "hallmarks" have survived to this day.

An account dating back to the reign of Elizabeth I recounts one of the earliest examples of trademark litigation on record: "A clothier of Gloucestershire sold very good cloth, so that in London if they saw any cloth of his mark they would buy it without searching thereof; and another who made ill cloth put his mark on it without privity; and an action was brought by him who bought the cloth, for this deceit; and adjudged maintainable."

is fairly clear. Registration of a mark is absolutely prohibited if, for example, it comprises immoral matter, deceptive matter, or scandalous matter; matter that may disparage or falsely suggest a connection with persons, institutions, beliefs, or national symbols; or matter that uses the flag or coat of arms of the United States, any state, any municipality, or any foreign nation.

In addition, the name of a living person may not be used without his consent, and the name of a dead President of the United States may not be used within the lifetime of his widow without her written consent.

Legalize My Name

Once the company has settled on a name and satisfied itself that it meets the legal requirements, it will probably want to register the mark in the U.S. Patent Office. Although this is not required, it does provide four definite advantages: (1) It gives notice to the world of your claim to the mark; (2) it creates presumptions as to ownership and the exclusive right to use; (3) it may represent conclusive evidence of the right to exclusive use; and (4) it may be used as the basis for obtaining registrations in foreign countries.

Unlike an invention, which may be patented whether it is used or not, a trademark must be in use before it can be registered. The owner of the mark must then submit a written application, setting forth the goods on which it is currently being used, accompanied by a drawing of the mark, five specimens or facsimiles, the date of its first use, and a fee of twenty-five dollars. If the application is allowed, the trademark will be published in the *Official Gazette* of the Patent Office to enable anyone who feels that he would be damaged by registration of that mark to file his opposition within thirty days.

Other Registrable Marks

Current trademark law also permits the registration of collective marks, certification marks, and service marks. A collective mark is used by members of a union, association, cooperative, or other group to indicate membership. A certification mark is used by others besides the owner to certify origin or quality—as, for example, the Good Housekeeping Seal of Approval. A service mark is a symbol or name used in advertising or sale of services to identify them. Greyhound and One Man's Family are registrable service marks, as are such slogans as "Sleep Like a Kitten" and "The System of the Flying Clippers."

Trademarks can also be registered in each of the fifty states and in most foreign countries. State registration fees range from a dollar to twenty-five dollars; a mark may be registered in all states for total fees of about $450. Marks are registered in perpetuity in fifteen

states; in others they are renewable after ten or twenty years. The renewal term of the U.S. Patent Office is also twenty years. Unlike patents and copyrights, which have a fixed term, trademark registrations are renewable indefinitely, as long as the mark remains in use.

If registering a trademark were enough to insure that it would be forever protected, it would be a comparatively simple matter; unfortunately, however, much more than this is necessary. A trademark gains its validity through use, not through registration, and it may be lost forever through misuse. This means that a continuous effort must be made to "police" the mark—within the company, within the trade, and in outside media.

Within the Company

It is imperative to be sure that company personnel understand the importance of using your trademarks correctly. There are three basic rules that everyone should follow:

1. Spell your trademark correctly at all times, and do not deviate from the established form of the mark, even in minor details. Everyone, from stenographers to artists and copywriters, should be aware that misspelling, altering accepted typographical treatments or proportions of elements in the mark, or combining it with other devices or words is inviting trouble.

2. Capitalize the first letter of the trademark—or, if you prefer, capitalize the entire word or set it off in quotes.

3. Be certain that you do not use your trademark as a description of your product or as the basic name of your product. The Du Pont company lost the right to the exclusive use of its cellophane trademark when it used the word to describe the article on which it was used. Similarly, aspirin, escalator, zipper, linoleum, and other trademarks have been held to be generic terms that anyone is free to use.

Clarifying Ownership

To avoid this possibility, it is well to add a descriptive term to the trademark whenever possible. Johnson & Johnson, for example, insists that the trademark Band-Aid always be followed by the words "adhesive bandages" or "the Johnson & Johnson adhesive bandage." And, when a registered trademark is used on packages, advertising signs and copy, television commercials, direct mail, stationery, business forms, and so forth, it is advisable to refer to the ownership of the trademark. This can be done by using one of the forms recognized by the Patent Office ("Registered in U.S. Patent Office," or "Reg. U.S. Pat. Off.," or ®). Some companies prefer to add the words "trademark" or "brand" to insure public understanding.

Many companies have distributed manuals of trademark usage, incor-

porating this type of information, to their employees. Among the companies that have found it worth their while to prepare such informational booklets are The Coca-Cola Company, General Motors, Eastman Kodak Company, Minnesota Mining and Manufacturing Company, Monsanto Chemical Company, and Westinghouse Electric Company.

Within the Trade

Policing the use of your marks within the trade is also important. Wholesale distributors, retailers, or persons licensed by the trademark owner to use the trademark should be aware of the principles of correct usage and the serious implications of carelessness in misusing it.

Some companies distribute informational material on these points to others who will be using their trademarks. A well-prepared style sheet can do much to eliminate confusion and insure that the trademark will be safe. Some require their regional representatives or dealer outlets to submit displays, advertising, or other promotional material that uses the trademark for approval. And many ask their salesmen and regional representatives to report to the home office any instances of improper use of the company's trademarks.

A CHECK LIST FOR TRADEMARK USAGE

A LEAFLET issued by the United States Trademark Association lists the following points to keep in mind when using your company's valuable trademarks:

It is correct to:

1. Use an initial capital letter.
2. Use the trademark as an adjective with a generic term for the product. For example: "Thermos vacuum bottles."

It is incorrect to:

1. Use a trademark as a plural noun. For example, "Band-Aid bandages" is correct; "Band-Aids" is improper.
2. Use a trademark as a possessive. For example, "Curity's fine quality" is improper; "the fine quality of Curity diapers" is proper.
3. Make a verb of a trademark. For example, "Addressographing" is incorrect; "Addressograph" is the trademark for repetitive writing machines.
4. Use the trademark of one company for the product of another company; it is the property of only *one* company.

Sample Letter to an Editor Who Has Misused the Company's Trademark*

Mr. Blank
a publication
Newark, N. J.

Dear Mr. Blank:

We want to thank you for the friendly mention of BAND-AID Adhesive Bandages in your publication of November. Such notice is flattering and we are extremely grateful.

Should you have occasion to do so again, however, we would like you to word your reference to our product a little differently in the interest of protecting our 34-year old trademark. BAND-AID is a Johnson & Johnson trademark and should not be used either in singular or plural form to describe a small bandage.

You see, we manufacture eight different products under this trademark. Furthermore, several other manufacturers make and sell similar small bandages under their own trademarks. Therefore, if you merely wish to indicate a little bandage, please say just "Plastic Strips" or "Adhesive Bandages," the usual descriptive names for these items.

In the interest of our customers as well as ourselves we want to avoid misuses of the very valuable BAND-AID trademark which we originated. Repeated misuses might cause it to pass into the language, where it might be used by competitors and imitators. As you may recall, this is what happened in the case of aspirin, cellophane, and linoleum, all once the trademarks of companies that originated these products.

Enclosed is a folder spelling out the legal technicalities involved. I am sure that you understand our feelings and will help us.

Sincerely yours,

JOHNSON & JOHNSON
Vice President

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* Reprinted by permission from *Trademark Management* (The United States Trademark Association, 6 East 45 Street, New York 17, N.Y.).

In most cases, of course, it is virtually impossible to check every use of the trademark, but regular procedures can be established to monitor advertising, promotional material, catalogs, service manuals, and other media in which authorized use of the trademark appears.

In Outside Media

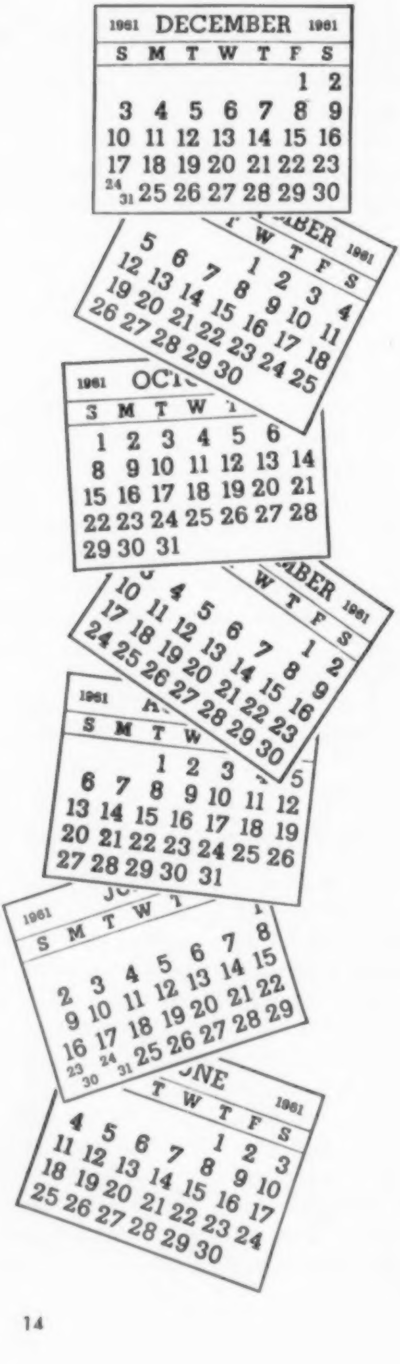
The third—and probably the most difficult—area to police is communications: newspapers, magazines, radio, television, and all other media that might mention a trademark. This is a sizable task; in addition to enlisting the help of regional offices and branches of the company, the use of clipping services that systematically examine such media is often a necessity. The company should have a central location to which all such gratuitous mentions are sent for classification and, when it is necessary, for positive action.

When a misuse of a trademark is found, the company should send a letter to the offender, explaining the importance of proper use of the mark and asking for future compliance with proper usage. It is wise to use a tactful and friendly approach, and to have the letter come from an executive who is not connected with the legal department. (An effective example of a letter to an editor appears on page 12.) Copies of all such letters should be kept on file, to be used if it is ever necessary to prove that you have exercised "due diligence" in protecting your right to your trademark.

Some companies have taken ads in trade and business publications to educate potential users and to stress the importance of observing the rules of correct usage. Others have sent speakers to conventions of editorial personnel to seek the cooperation of editors in protecting their trademarks. The benefits of guarding trademarks do not accrue exclusively to the manufacturer, either; it is well to remember that the press has an interest as well. As Robert U. Brown of *Editor & Publisher* has put it: "The constant misuse of a trademark by the press can in time undermine and destroy its usefulness and value. Promotion of trademark and brand name products is the keystone of modern advertising. Editors have a selfish interest in trying not to kill the geese that are laying those golden eggs."

Worth the Candle

Never has there been a time when trademarks have been so valuable—and when their loss could be such a substantial blow to a company's competitive position. It is clear that the process of choosing a trademark, publicizing it, and keeping it protected is a difficult and continuing one; it is equally clear, however, that it is a task that has become of vital importance to companies doing business in the competitive markets of the nation and of the world. ♦



The Case for the NATURAL BUSINESS YEAR

Condensed from
Trends in Management-Stockholder Relations

THE SEASON of annual meetings is almost here. And each year, the season's problems grow worse: The number of stockholders continues to increase; the amount of stock in brokerage name continues to rise; brokerage proxy departments are under ever-increasing pressure; and more and more companies solicit proxies. Further, the flood of proxy

Trends in Management-Stockholder Relations (October 1961), Georgeson & Co.

material to be cleared by the SEC keeps rising, and the problem will be greatly compounded if the thousands of unlisted companies are ever made subject to the proxy rules.

Force of Habit

It may be well for corporations to consider, in their own interests, what might be done about the annual-meeting problem. Briefly stated, the problem is that too many corporations close their books on December 31. This closing date is now merely habit with many corporations and is retained on that basis alone. In some cases it is linked to former government action: In 1909, an excise-tax law required corporations to file reports to the government for the calendar year as opposed to a fiscal year that may have been used previously. The revenue laws of 1913 allowed companies to resume filing tax returns on a fiscal-year basis, but many companies stayed with the calendar-year basis.

The natural business year is the period of twelve consecutive months ending when a business's activities reach the lowest point in its annual cycle. There are many advantages to using a natural-business-year closing. Most companies operate on a yearly cycle; when the books are closed at the lowest point of business activity in the cycle, several aspects of determining profit are simplified. Inventory-taking, for example, is a major hazard in preparing a financial statement. In many industries, midwinter is the peak production season and temporary employees working overtime must be used to take inventory. Use of the natural business year permits regular employees to be used with a minimum of interference with production. Since inventory is at its lowest level, it becomes easier to assign overhead, and less cost is deferred to a subsequent period. In addition, the low level of inventories permits a much more accurate auditing check.

At the end of the natural business year, accounts receivable, accounts and notes payable, and inventories are at their lowest points, while cash balance is larger than at any other time of the year. The working-capital ratio is highest and the liquid position is the most favorable; thus the balance sheet reflects maximum fact, minimum opinion.

The use of the natural business year also eliminates the overlapping of work connected with the closing of the books on December 31 and the concurrent compilation and filing of the numerous reports required by the government.

Changeover Conditions

Changing to a natural business year does not require permission from the Internal Revenue Service if:

• The corporation has not changed its accounting period at any time within a ten-calendar-year peri-

od, the end of which includes the beginning of the short period required to effect the change that is proposed.

- The short period required to effect the change is not one in which the corporation would show a net operating loss.
- The taxable income for the short period is, when annualized, at least 80 per cent of the taxable income for the preceding taxable year.
- A corporation with a special status (such as a personal holding company, a foreign personal holding company, etc.) has maintained the same status for both the short period and the preceding taxable year.

Not every company can or should use the natural business year. Its adoption should be based on sound business reasoning and on a thorough study of all the factors that are involved. It is possible that its use could lead to certain disadvantages where the creation of a short taxable year reduces the period of availability for existing capital-loss carry-overs, contribution carry-overs, and operating-loss carry-overs; where the short taxable year would have the effect of accelerating federal income taxes and estimated income-tax payments; or where an inventory system would present a serious obstacle. ♦

The Shortage of Managers: A World-Wide Problem

A SHORTAGE OF QUALIFIED MANAGERS is seriously delaying the potential growth of business throughout a large part of the world, according to an eight-nation study recently released by the National Industrial Conference Board.

Although the shortage is a world-wide problem, the precise nature of it differs from country to country. The more highly industrialized nations need managers who can conduct the large and complex businesses that are beginning to characterize the economies of those countries. In nations where industrialization is fairly recent, resourceful managers are needed to guide new economic units.

In France, for example, traditional management methods are being challenged by new competition and opportunities resulting from the European Common Market. In India, many companies were originally developed under a managing-agency system or as subsidiaries of foreign concerns; now, with the establishment of Indian companies, there is considerable interest in management training. The copper-dominated Chilean economy has been shaken by sharp recent declines in world copper prices. An ambitious ten-year development plan, aimed at industrial expansion and diversification, has been drawn up, but its goals cannot be reached without a considerable increase in the supply of trained managers.

Other nations surveyed in the study were Great Britain, Germany, Italy, Japan, and the United States.

Europe's Growing Economy—Needs and Prospects

Condensed from Business Week

AN ALMOST PHENOMENAL growth of the European economy by the end of this decade is mapped out in great detail by a new Twentieth Century Fund study, *Europe's Needs and Resources.* The massive 1200-page study traces Europe's postwar recovery and then projects its growth from 1955 to 1970. As the first comprehensive look at 1970 to be published, it will doubtless serve as a bench mark for market researchers and economists for several years to come.

The study's implications are tremendous for U.S. companies manufacturing in Europe, for those doing business in almost any part of the world, and for economists concerned with the U.S. balance of payments in coming years. Here are some of the conclusions that can be drawn from the Twentieth Century Fund projections:

- Europe will increasingly become a prize market for U.S. companies that produce within its borders—and, of course, for European companies themselves.
- To some extent, U.S. exporters will find a growing market in Europe, but the share of finished goods in Europe's total imports will be crimped, placing a greater premium on the ability to manufacture there.
- U.S. exports of basic farm commodities to Europe will probably decline drastically by 1970.
- In third markets—mainly the less-developed countries—European exports will be a strong threat to U.S. products, particularly in capital goods.
- Europe in 1970 may have a serious problem regarding its combined balance of payments. Its needs for imported raw materials and fuels will be so great that even an optimum performance by European exporters, as projected in the

study, will leave a payments surplus relatively weaker than that of today. And if European exporters slacken their efforts, the projected surplus could be much weaker.

Europe's GNP

The key indicator of growth is the gross national product. For Western Europe as a whole, this is expected to mount to 342 billion dollars by 1970, up 54.8 per cent from the 1955 base of 221 billion dollars. (All 1970 figures are deflated, however, in that they are estimated in 1955 prices.)

The marketing implications are spelled out by GNP per capita. Because Western Europe's population will rise by 8.4 per cent to a total of 320 million persons by 1970, per-capita GNP will increase by a smaller percentage than total GNP. But it will still rise to $1,067, up 42.8 per cent from 1955's $747.

By 1970, Europe's richest markets in terms of per-capita GNP will be virtually the same ones as today: Switzerland, Sweden, Belgium, Luxembourg, and Britain. Gains will be greatest in Italy, France, Austria, and Sweden, less in Britain and Germany; other countries' per-capita growth will fall in between.

Consumer spending will rise faster than GNP, accounting for a larger share of GNP in 1970 than it does today. Over-all it will rise to 230 billion dollars, up 59 per cent from 1955's 145 billion dollars. Per capita, the projected 1970 average of $719 will be 46.7 per cent above the base-year (1955) average of $490.

Here again there will be great variations among countries: Per-capita spending will range from $460 in the low-consumption countries (such as Spain, Greece, and Italy) to $925 in high-consumption nations (such as Sweden, France, and Britain).

Spending for all major consumer items will rise in absolute terms as per-capita spending expands. But the share of the total going to some items, such as food, will decline, while that of others, such as clothing, will remain about the same. Receiving a bigger share of each citizen's pocketbook will be such items as housing and durable goods. Per-capita spending for housing will rise from $33 to $51; for furniture, it will rise from $15 to $23. For appliances, per-capita spending will nearly double, from $14 to $27, and for autos it will more than double, from $9 to $22.

U.S.-Style Economy

This increase in spending for autos will mean a tripling of the passenger-car population—from 11.9 million in 1955 to 36.5 million in 1970. Along with the rise in other durables, this suggests that Europe will be approaching a U.S.-style economy. As in the U.S., the auto will become a major economic factor, with annual sales of some five

million dollars approaching America's present-day rate, and with a growth of service industries based on the auto.

There are other indications of an "Americanization" of Europe's economy by 1970. Education, for instance, will begin reaching into the 15-to-19-year age group. As more European youths continue their studies in secondary schools and beyond, total spending on education will soar to 9.2 billion dollars, up 73 per cent from 1955's 5.3 billion dollars.

In such areas as food consumption, a U.S.-type trend is also under way. As a higher proportion of women join the work force, and as the number of domestic servants declines, eating habits are almost sure to shift to more "convenience" foods.

Trade and Capital Spending

In order to achieve this growth in production and personal income, Western Europe must plow back a sizable portion of GNP into capital investment. As the share of GNP going into consumer spending rises, capital formation's share will decline slightly—from 20 per cent in 1955 to 18 per cent in 1970. But in absolute terms the total will rise from 45 billion dollars to 63 billion dollars. This implies a continuing healthy market for capital goods and construction.

The weak point in Europe's growth may turn out to be its foreign trade, for Europe's imports of raw materials and fuels will soar to feed this growth. The share of food in its imports will decline, and the percentage of manufactured goods may decline or remain steady. But these will be offset by rises in the share of the import bill that is going to ores, base metals, and fuels.

Europe's Energy Needs

Europe's energy needs that cannot be met internally, measured in terms of tons of coal, will rise from 182 million tons in 1955 to 425 million in 1970. Of this need, 25 million tons are expected to be met by imported coal and the rest by imported oil. This could mean a fuel bill of seven billion dollars, double the 1955 figure—and that's a conservative estimate. It could easily mount to nearly nine billion dollars, the study indicates.

Thus Europe's imports will rise at least as fast as its exports. Europe's total trade with the rest of the world in 1970 will break down into exports of 23 to 24 billion dollars, and imports of 25.5 to 27 billion dollars. The trade deficit will be offset, as it is today, by an estimated five-billion-dollar income from such "invisibles" as shipping, insurance, and tourism. This would leave a surplus on current account of some two billion dollars, about double the 1955 figure. By last year, Europe's surplus had just about reached this favorable figure, in terms of 1955 prices.

If, however, Europe does no better than this by 1970, it would mean a weaker payments position. Today, most of Europe's favorable balance is stashed away in reserves, but by 1970 the Europeans will be almost forced to invest most of their surplus abroad—partly to develop export markets and partly to develop foreign natural resources to provide the raw materials and fuels they will require.

The study makes it clear that its estimates of exports by 1970 are on the optimistic side. Whether these figures are achieved will depend largely on how much Europe invests to create markets for itself in the developing countries of Asia, Africa, and Latin America. ♦

Cesium: A Key Metal in the Space Age

CESIUM—an often rejected metal—may become a key material in U.S. attempts to reach the planets, reports *Steel.* Cesium is a true space-age metal; all its potentials rest on techniques and technologies undreamed of a few years ago.

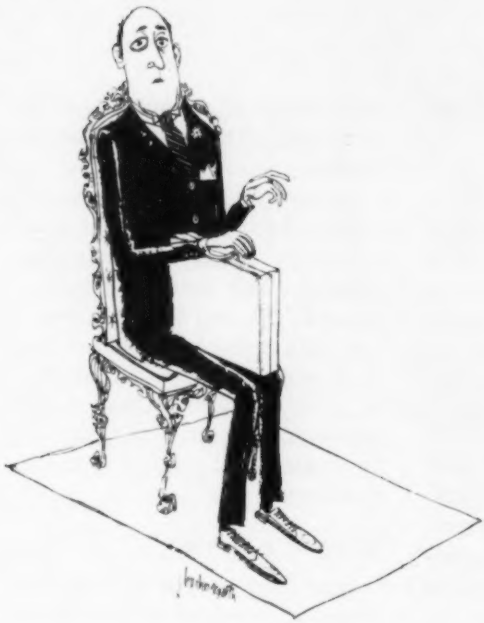
Few metals have a greater combination of undesirable characteristics. Cesium will melt from the heat of your hand. It explodes on contact with water. When exposed to air, it instantly bursts into flame. It's the softest, but also the heaviest, of the alkali metals. And it's worthless as a structural metal.

However, cesium has one big plus over the stronger, more stable metals: It has the greatest tendency to ionize of any metal. All its uses are based on this property.

The National Aeronautics & Space Administration is planning to test an ion-propelled space vehicle. Outside the earth's atmosphere, an ion engine propels a ship through space by shooting a stream of ions through an exhaust. Cesium vapor is ionized by passing it through a heated plate of porous tungsten. An electric or magnetic field accelerates the ions. Shooting out the exhaust at about 300,000 miles an hour, they give the spacecraft its push.

Cesium is playing a key role in the development of two power-generation systems: magnetohydrodynamics and thermionic converters. MHD works on the principle of utilizing a conducting plasma at high temperatures within a magnetic field to generate electricity. Cesium contributes to the ionization of the plasma and lowers the temperature at which the MHD generator can be operated.

A thermionic converter generates electricity by the flow of electrons from a hot surface to a cold one. Cesium, when ionized, provides the electrons with a path between a cathode and anode—much the same way as lightning is the ionized path for electrons between a charged cloud and the earth.



When the Security Analyst Comes to Call

By Maxwell R. D. Vos

Condensed from Dun's Review and Modern Industry

"I DON'T UNDERSTAND Wall Street," lamented a well-known industrialist, "and they don't understand me." Many a corporate officer echoes this statement—particularly when the security analyst comes to visit. Some executives choke up entirely in the security analyst's presence; others try to play a game of informational hide-and-seek; and still others show him so much that he ends up hardly knowing if the company is solvent or not.

Just how does an executive properly receive an analyst? What should he tell him? What information can he justifiably prevent the analyst from learning? And how does he enlist the analyst's support and understanding so that the company

Dun's Review and Modern Industry (November, 1961), © 1961 by Dun & Bradstreet Publications Corporation

and its stock will get a fair break in the market?

Talking to Wall Street

Talking clearly to Wall Street is no simple task. To succeed at it, businessmen should keep three objectives of financial public relations in mind:

- The businessman must attract support from investment-banking firms, in preparation for the possible issue of new securities. Every company seeks such support, of course, when new bonds or stock are actually authorized for sale, but few businessmen plan for a continuing effort.
- Executives must make sure that Wall Street understands management's policies and the reasoning behind them. Any company can get entangled in a proxy fight; when that happens, it helps to have the good will of the professionals in the investment business.
- Every company has a vital interest in encouraging a fair valuation of its stock in the market. The only way to do this is to disseminate and explain all relevant facts and figures that do not have to be kept under wraps. This third objective embraces the two others, and—simple as it is—few businessmen understand its implications. "What do I have to do with the price of the stock?" asked one company president. "My business is to look after the earnings and the balance sheet. Let the brokers worry about whether we're worth fifteen times earnings or twenty." This is an unprofitable attitude.

Suppose your company earned $2 a share last year, and sold at an average price of 30, or fifteen times earnings. This year you expect to report $2.50, and if the price-earnings ratio remains unchanged your stock will sell at 37½. Thus you'll be able, in effect, to present your shareholders with $7.50 for each share they hold, taxable at capital-gains rates.

Value of a Program

Now suppose that this year you initiate a sound financial public-relations program. You invite a number of analysts to see the plant and talk to the officers. Perhaps you arrange to address one of the component groups of the National Association of Financial Analysts' Societies. You bring out certain facts about your company which are not widely known.

You tell them, for example, that the 25 per cent earnings improvement projected for this year is typical of the past decade, during which your company has grown at an average rate of 20 per cent a year compounded. "The quality of our earnings is improving," you explain. "Five years ago, our ten largest customers accounted for 35 per cent of our total sales. Today, our twenty largest customers account for only 23 per cent. Two-thirds of our sales are in products we didn't even

make before 1954. Our sales of replacement and maintenance parts now make up 20 per cent of the total and the percentage is rising every year, so we are becoming less dependent on the business cycle."

As these facts get around, Wall Street may take a new look at your stock. The price-earnings ratio may begin to creep up to 17, 18½, 20. When it becomes clear that your $2.50 estimate for the current year is realistic, your stock could well be selling in the neighborhood of 50.

Consider what you have accomplished. Merely achieving your earnings goals would have brought $7.50 a share to your stockholders. But by capitalizing on that achievement through a program of financial public relations, you have increased the value to $20 a share.

This process, of course, can be carried too far. A stock that is "talked up" without a substantial basis of continuing merit will inevitably come down. And it is probably better to let the stock work its way up to 37 or 40 than to talk it up to 50 and then see it collapse 15 points in the next market correction.

Image-Building

Honorable and successful "image building" involves a few simple principles. First, be honest in dealing with analysts. You are not obliged, of course, to tell them anything you would not tell a competitor; remember, however, that you aren't talking to a competitor. Perhaps you have attached a "classified" label to some information that is not really confidential. If so, consider taking off some of those wraps. Try not to hide more than you have to. And above all, do not attempt to conceal bad news. A poor quarterly-earnings statement will hit your stock far harder if it comes as a complete surprise to the financial community.

What to Avoid

Don't go the other extreme, however: Avoid forcing more information on an analyst than he wants or can use. For example, don't take him on a tour of your plant without making sure that he would like it and can profit from it. If he does express an interest, try not to subject him to technical discussions; unless he is a specialist, he probably won't understand.

Don't try to force conclusions about your company on an analyst; conclusions are his business, not yours. On the other hand, ask to see his finished report before it is released. You are justified in asking to check it for factual accuracy, and if you think his findings are way off base, you will have the opportunity to explain your point of view.

Finally, if you want your stock to be fairly priced in the market, keep yourself informed on Wall Street's current attitude toward your company. If you think it is misconceived, be frank in saying so—and do your best to correct it. ♦

SERVICE with a *SELL*

Richard W. Harbison
Vice-President and Division General Manager
Service Division
Lear, Incorporated

NOT TOO LONG AGO, product service was widely considered a necessary evil at best, to be given as little time and attention as possible. Today, however, many companies are finding that service can be a decided asset—a prime source of additional sales volume and profit. In some firms, profit from the service operation alone has been substantial; more often, however, the profit from improved service has been modest in comparison with the profit resulting from the increased sale of products.

Why has service become so important in the over-all marketing picture? For one thing, the products themselves have obviously become much more complex. Automobiles have power steering, power brakes, high-compression engines, automatic transmissions. The housewife's electric iron has been all but replaced by the much more complicated steam iron. Washing machines are replete with controls for different water temperatures, cycles, and speeds. In the industrial field, production equipment has become

A MANAGEMENT REVIEW SPECIAL FEATURE

more and more automatic and intricate.

This general increase in the complexity of products, and hence in their susceptibility to malfunction and breakdown, has been accompanied by a growing customer demand for good product service. No longer is it possible, as it was immediately after World War II, to sell products on a take-it-or-leave-it basis and ignore or neglect service; today's consumers are turning away from companies with a poor record for service and demanding an assurance of good repair and maintenance almost as a condition of sale.

Expanding Sales Volume

But service is more than a competitive necessity; many companies have found it a means of reaching untapped sales volume.

The Worthington Corporation, which manufactures air hammers for contractors, was able to boost its sales 25 per cent recently in the face of an industry sales decline of almost 19 per cent through the addition of a service unavailable elsewhere. By installing a plan whereby customers could borrow a Worthington tool while their own was being repaired, the manufacturer solved one of his customers' most annoying servicing problems—how to keep costly down time to a minimum without investing heavily in costly stand-by equipment. Lear, Inc., a manufacturer of aerospace systems and equipment, does the same thing with certain of its commercial aircraft equipment.

Lear decided in 1959 that an enlarged service operation could provide additional profit, as well as important customer benefits. When service sales rose from less than a million dollars to two-and-a-half million dollars during the first year, the company set up a separate service division—and business doubled again. In 1961, Lear expects a volume of from six to seven million dollars from its service operation.

The Addressograph-Multigraph Corporation of Cleveland expanded its profitable product-service operation when it found that companies that purchase its products are receptive to service contracts in which the company's serviceman makes regular stops at the offices where the equipment is operating. The serviceman lubricates and cleans the equipment, replaces worn parts, and notices opportunities for preventive maintenance.

These are but a few of the companies that have already discovered that an efficient service operation can help the balance sheet.

A Competitive Weapon

One of the many benefits of efficient service is the strong weapon it provides against aggressive competition. Volkswagen has continued to expand its U.S. operations despite the strong competition from American compact cars, and most pundits

"A good service operation is also an invaluable means of obtaining information on product performance in the field . . . Service can identify market needs that suggest new products, different products, or new applications for existing products. . ."

• • •

in the automotive field believe that the company's excellent service facilities across the country have played a key part in enabling it to meet competition. The major U.S. automotive producers, of course, have long maintained nationwide service facilities; in fact, the manufacture and distribution of replacement parts has been an extremely profitable segment of their business.

Good service helps a company to meet competition without resorting to ruinous price-cutting. In the past decade, for example, the Singer Sewing Machine Company has faced extremely difficult competition from lower-priced foreign-made sewing machines. Company officials credit Singer's ability to successfully maintain its price structure in part to the vast service operations the company conducts from coast to coast, which assure the customer that a Singer sewing machine need never be idle for lack of parts or a knowledgeable serviceman to repair it.

A good service operation is also an invaluable means of obtaining information on product performance in the field, since even the most careful product testing in the factory occasionally fails to uncover bugs that turn up in actual use. Westinghouse has found this information so important that it calls its service managers back to the home office from time to time to help plan the company's line of washers and dryers. A good service operation can also provide information on how competitive products operate in the field—their strengths and their weaknesses.

Turnabout Is Good Business

Victor Petchul, editor of *Appliance Manufacturer*, reports that the major appliance industry has undergone a turnabout in its attitude toward service in the past ten years: "Formerly, the companies rarely, if ever, publicly acknowledged that their products might need future service. Today, service has come of age. Service managers actively participate with product engineers and marketing people in product planning. In many instances, the service department actually can exercise a veto on releasing the product for

manufacture unless it meets service considerations."

New Products, New Markets

Service can identify market needs that suggest new products, different products, or new applications for existing products. Shortly after Modine Manufacturing Company of Racine, Wisconsin, expanded its product-service operation, there was an epidemic of noisy Modine gas unit heaters in southern schools. Since the units had been designed originally for industrial and commercial installations, where the quantity of heat produced was more important than quiet, it was apparent that the product had been misapplied. It was also apparent, however, that the school field was a major market area that had been neglected. Modine designed a new shock-mounting to isolate vibration and reduce noise, and all the existing heaters in schools were replaced with the improved product. As a consequence, the company earned the good will of its school customers and, in addition, opened up a whole new market for itself.

Profitable Service

Effective service doesn't just happen; it requires planning and hard work. Although each industry has its own peculiar conditions that affect profit, a number of considerations common to most industries are of importance in insuring the profitability of service operations. The eight areas discussed below should receive particular attention.

Warranties. Some companies provide warranties on their product far in excess of ethical obligations, what the consumer pays for, or what competition requires. Excessive warranty commitments can turn any service department into a losing operation.

Costs. The secret of service, like so many other aspects of business, starts with knowing costs. It is essential that the accounting system separate costs into their fixed and variable components. If the company doesn't know what its service billing procedure costs, for example, it cannot possibly recognize that it may cost three dollars to process a seven-dollar job. The paperwork of a service operation must be geared to the activity level of the operation: A small-volume operation should have little or no expensive equipment and a minimum of different pieces of paper that have to be filled out, recorded, and analyzed.

It is essential, of course, for a service activity to have an adequate supply of spare parts, but this objective must be consistent with the costs of carrying inventory. It has been estimated that it costs approximately 15 to 20 per cent of the true value of an inventory item to carry it in stock for one year.

The service facility need not be in the center of the town; it can be located where the cost of rent and buildings is low. Analyze the pro-

portion of factory service, factory-field service, and dealer service that should be included in your over-all service mix. Factory service cannot operate profitably in areas where product concentration is low unless the unit cost of the product is extremely high. Factory service is most effective and profitable where there is a high concentration of customers; otherwise, branch or dealer service is indicated.

Pricing and Product Design

Pricing. The price of service must be set with full knowledge of what competition is charging for comparable service and an analysis of the cost of the parts and the labor that go into the service operation. The cost of service parts is higher than the cost of parts for production because it must include the cost of the time the part sits on the shelf. Charles Hawkins, vice-president of Industrial Technological Associates, indicates that in a large number of instances, companies have found that the price of a service part must net about twice what the same part would get if used in production.

The price of labor generally should not be less than two-and-a-half times its cost. Most consumer hard-goods manufacturers estimate that it costs more than six dollars an hour to keep a serviceman on the street. This includes wages, truck operating costs, some overhead, but no allowance for profit or special expenses. In lines where the product has a high scientific content, the cost of service labor is substantially greater.

Product design. When a product is not designed for efficient service, a manufacturer may find himself with a consumer revolt on his hands if he attempts to charge what it costs to repair the product. Some supposedly sophisticated manufacturers still make products that can be opened only by breaking them apart or by drilling out the rivets or other fastenings. Many products have to be torn down to clean or repair minor parts.

The basic requirements for easy servicing include these four:

- Make small parts and subassemblies replaceable.
- Make component parts easily accessible and easy to replace.
- Standardize nuts and bolts.
- Minimize the use of fastenings that have to be destroyed in order to separate various parts.

Training Customers and Servicemen

Train customers in the use of your products. Customers often tend to try out a new product before reading the instruction book. They overload the washing machine; they mistake humidity vapor from their refrigerator for smoke; they make frantic calls to the serviceman before checking the plug. It has been estimated that one-fourth of all service calls are actually unnecessary.

It is essential that the sales staff

recognize the importance of educating the customer in the use of the product. Reliance Electric and Engineering Company of Cleveland offers a five-day training period in their office or in customers' plants for personnel who operate Reliance motor drives and controls. The company has found that this improves customer satisfaction with the product and, of equal importance, reduces costly and unnecessary service calls.

Train your service personnel. Customers complain justifiably if the serviceman has to return a second time to do the job right. The serviceman must be well trained in

"What have you been doing for the past eleven months?"

the care and maintenance of your products. Efficient work standards should be established and wage incentives provided for personnel whose performance is above the minimum standards.

Good service manuals are also required. They should include an easily interpreted parts list, operating instructions, maintenance information, and complete overhaul data. All copy should be written simply, with a minimum of complex technical and engineering terms. Some companies make the mistake of having their manuals produced by the parts department, forgetting that most parts clerks are neither writers nor mechanics. In other companies, engineers alone are entrusted with the preparation of the service material, and the manual is over the heads of the less-educated service mechanic. Good graphic material can go a long way to simplify complicated service techniques.

Optimum Use of Servicemen

Planning for optimum utilization of service personnel is important. In areas where there is a high concentration of service business, some companies utilize vehicles with two-way radios to speed their servicemen to each succeeding assignment.

Where possible, enter into continuous service agreements with customers. Sears, RCA, and other consumer appliance companies have had success with this. A service contract can reduce charges to customers as well as increase service possibilities. When servicemen can spend a majority of time on planned service routines, substantial savings result. There is a minimum of idle time, and down time in the customer's facility is reduced. In addition, the use of localized routes permits transportation costs to be prorated among customers in the area.

Organization

Coordinate the service operation with other activities of the company, but keep it separate. Sales should make service a part of its pitch, but never a part of its operation. When service is subordinated to sales or manufacturing, service is rarely as prompt as it is in a service department for which servicing is the priority consideration. This is quite understandable, for the priorities of the manufacturing or sales departments are different.

Coordination with other areas of the company, however, is feasible and necessary. For example, the cost of service parts can be prohibitive unless they are scheduled for manufacture along with a regular production run, thus eliminating the expense of future short-run manufacture with its special tooling and set-up costs.

Expanding Operations

Consider expanding the service operation. Many companies can expand their service operation profit-

ably. First, however, an analysis of outside groups that are now serving your products is necessary. What dollar volume is involved? Is it economical to pull this volume back into the house?

Second, look for any lack of service capability in your industry that might offer an opportunity for expansion. Singer Sewing Machine, for example, services not only its own sewing machines but those of competitors as well.

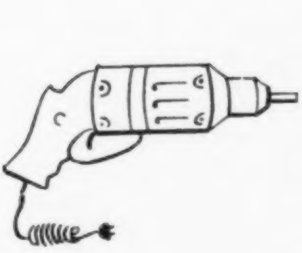
Third, examine the long-term trends in your industry. Will it be more desirable in the future to service rather than replace existing products?

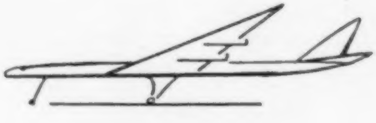
Fourth, determine whether your existing volume will grow to the point where expanded service will be required.

Fifth, examine the product-design trends in your industry. As products become more complex and have a higher scientific content, specialized skills for service are often required. Customers may find that it is easier to hire these skills from you than to maintain and repair equipment themselves.

Service with a Sell

Even if the service operation were not profitable, many companies would find it difficult indeed to keep their customers happy—and to keep them customers—without it. But it's seldom necessary to make a choice between losing money and losing customers. Properly organized and handled, service can be a profitable operation in itself—and it can return its cost many times over by attracting new and profitable sales volume. So many companies have found this to be true that product service is becoming one of industry's most valuable sales tools. ♦





EFFECTIVE PLANNING:

Does Management Have the Information It Needs?

By D. Ronald Daniel

Condensed from Harvard Business Review

THERE IS HARDLY a major company in the United States whose plan of organization has not been changed and rechanged since World War II. With revised structures have come new jobs, new responsibilities, new decision-making authorities, and reshaped reporting relationships—all of which combine to create new demands for information.

Management needs information in order to set objectives, shape alternative strategies, make decisions, and measure results against planned goals. Unfortunately, management often loses sight of the simple relationship between organization structure and information needs; companies seldom follow up on reorganizations with penetrating reappraisals of their information

systems; and managers—who must translate statements of their new duties into action—often do not receive all the data they require.

In order to plan effectively for the future, management needs three basic types of information: *environmental information* (describing the social, political, and economic aspects of the climate in which a business operates or may operate in the future); *competitive information* (explaining the past performance, programs, and plans for competing companies); and *internal information* (indicating a company's own strengths and weaknesses).

Environmental Information

Environmental data form one of the least formalized and least used categories of management information. Specific examples of environmental data are:

- Population: current levels, growth trends, age distribution, geographical distribution, effect on unemployment.
- Price levels: retail, wholesale, commodities, government regulation.
- Transportation: availability, costs, competition, regulation.
- Foreign trade: balance of payments, exchange rates, convertibility.
- Labor force: skills, availability, wages, turnover, unions.

To these data, a company operating internationally would add the information—systematically collected and interpreted on a country-by-country basis—on political and economic conditions in the foreign areas where business is being done.

To be of maximum use, environmental data must indicate trends. Population figures, balance-of-payment data, or political shifts are of little significance when shown for one period because they don't help management make analytical interpretations.

Competitive Information

Data on competition comprise the second category of planning information. There are three important types to consider:

- *Past performance.* This includes information on the profitability, return on investment, share of market, and similar aspects of competing companies. Such information is primarily useful in identifying one's major competitors, and it serves as one bench mark when setting company objectives.
- *Present activity.* This category covers new-product introductions, management changes, price strategy, and other current developments in competing organizations. Good intelligence on such matters can materially influence a company's planning; for example, it may lead to accelerating research programs, modifying advertising strategy, or switching distribution channels. A company's plans, of course, should not be merely defensive and prompted by a competitor's moves; but

anything important a competitor does should be recognized and considered in the planning process.

• *Future plans.* This includes information on competitors' acquisition intentions, facility plans, and research-and-development efforts.

Internal Information

The third and final basic category of planning information consists of internal data. Such information is aimed at identifying a company's strengths and weaknesses —the characteristics that, when viewed in the perspective of the general business environment and in the light of competitive activity, should help management shape its future plans. It is useful to think of internal data as being of three types:

• *Quantitative-financial*—such as sales, costs, and cost behavior relative to volume changes.

• *Quantitative-physical*—for example, share of market, productivity, delivery performance, and manpower resources.

• *Nonquantitative*—such as community standing and labor relations.

In reporting internal data, a company's information system must be discriminating and selective. It should focus on "success factors"—those few key jobs which must be done exceedingly well for a company to be successful. In the automobile industry, for example, such factors are styling, an efficient dealer organization, and tight control of manufacturing costs. In food processing, they are new-product development, good distribution, and effective advertising. In life insurance, the development of agency management personnel, effective control of clerical personnel, and the creation of new types of policies are the important elements.

A large oil company, focusing on such a factor, devised a system of regularly reporting its "finding" costs—the ratio of the costs incurred in exploring for new reserves of oil to the number of barrels of oil found. When this ratio rose beyond an established point, it was a signal to the company's management to consider the acquisition of other oil companies (together with their proved reserves) as a less expensive way to find oil.

Management Reports

If a company is to have a comprehensive, integrated system of information to support its planning process, it will need a set of management reports that regularly covers the three basic categories of planning data—environmental, competitive, and internal. The amount of data required in each area will naturally vary from company to company and will depend on such factors as the nature of the industry, the size and operating territory of the company, and the acceptance by management of planning as an essential function. However, it is important in every case

for management to formalize and regularize the collection, transmission, processing, and presentation of planning information; the data are too vital to be ignored or taken care of by occasional "special studies."

Planning vs. Control Information

Management often assumes that the information it gathers for control functions will be suitable for its planning functions. However, the characteristics of planning data differ from those of control data in several ways:

- *Coverage*. Good planning information is not compartmentalized by functions: It seeks to transcend corporate divisions and to provide the basis on which integrated plans can be made. In contrast, control information hews closely to organizational lines so that it can be used to measure performance.
- *Length of time*. Planning information covers fairly long periods of time—months and years rather than days and weeks—and deals with trends. Thus, although it should be regularly prepared, it is not developed as frequently as control information.
- *Degree of detail*. Excessive detail is the quicksand of intelligent planning. Unlike control—where precision and attention to current detail do have a place—planning (and particularly long-range planning) focuses on the major outlines of the situation ahead.
- *Orientation*. Planning information should provide insights into the future. Control information shows past results and the reasons for them. ♦

"Be My Guest"

"BE MY GUEST," says one supervisor to another at General Motors Corporation (Linden, N. J.), and he means it. It's part of a training program to familiarize supervisors and general foremen with one another's problems, reports *Factory*.

Two supervisors, with little or no direct contact on the job, alternate host and guest roles weekly. For one hour, the guest sees his host in action. He discovers different ways to solve common problems. And he can better understand how other functions fit into the total plant activity. Later in the week, the two supervisors exchange roles.

Other benefits accrue from this two-hour training session. It improves plant teamwork concerning planning, quality control, and cost control; human and labor relations; absenteeism control; and record keeping. Furthermore, the supervisors almost unanimously favor the program and believe it to be beneficial.

Bonanza in Boxtops:

THE PREMIUM PICTURE TODAY

By Harry Woodward

Condensed from Sales Management

OVER ONE HUNDRED years ago, B. T. Babbitt offered housewives a lithographed picture for 25 wrappers from his soap. In 1900, Quaker Oats started packing a piece of chinaware in each large box. And a few years later, one manufacturer offered marketers an unusual sales aid: a noiseless soup spoon.

From such humble beginnings, premiums have grown to a 2.5-billion-dollar business. Premiums are now offered by companies in almost every consumer-goods field, on retail and wholesale levels alike. And many companies, while not offering premiums, are profitably engaged in manufacturing them.

Types of Plans

National Premium Sales Executives (NPSE) lists many types of premiums:

• *Self-Liquidators* are built around items offered—usually against mail response—to consumers who submit proof of purchase of a product. Most such offers are at 50 cents to $1 (including mailing fees), but many go for 25 cents or for $2 and more. Quantities range from 10,000, offered by small companies on a local or regional basis, to the rare million-plus. A national advertiser generally aims at 250,000 to 500,000. The most successful premium merchandise meets several requirements: It has broad appeal, is easy to sell through media, preferably needs no demonstration, and is easy to mail at low cost.

• *Coupon plans* are offered by many manufacturers of consumer products, who pack coupons with each unit and redeem them for premiums listed in a catalog. Items range from low-cost household goods to luxury items, and they usually appeal to all members of the family.

Sales Management (September 15, 1961).

• *Dealer premiums* are used to stimulate retailer sales of a manufacturer's product. Some companies have continuing coupon plans for dealers, with a coupon in every case of the product and a catalog of premiums.

• *Direct premiums* are the basic premium technique. A premium item is given directly to the consumer with the purchase of a product. It may be attached to the product package, enclosed with the product in a separate carton, enclosed inside the product package, or given to the consumer by the retailer. Or the package itself may be a "container premium."

• *Traffic-builders* are used primarily by retailers, but their use may be planned by the manufacturer for dealer promotion. The premium is advertised to consumers as a gift for visiting the store, viewing a demonstration, or some other action that benefits the retailer.

"Use the User"

• *Use-the-user plans* involve offers, by retailers of appliances and other direct sellers, of merchandise as a premium to an already-sold customer who recommends friends who, in turn, become customers. Sometimes the customer may be given a less valuable premium for simply providing a list of potential customers.

• *Trading stamps* are the principal form of premium used by retailers, particularly in the food field. With each ten-cent purchase, customers receive one stamp to be pasted in a booklet redeemable for merchandise from a catalog. A stamp plan usually is not run by the retailer but by a service organization which sells stamps to the stores and maintains merchandise for redemption. There are more than 300 such companies in the U.S.

• *Tape-redemption plans* are used by some supermarkets that don't want to bother with the long-range trading-stamp program. Customers' cash-register tapes are redeemable by customers for merchandise, sometimes upon payment of small cash amounts equal to the wholesale cost of the premiums. Small appliances and other housewares are the most common premiums, but soft goods are growing more important here.

• *Direct-sellers* are "door-opener" premiums, used by manufacturers who sell to housewives in their homes. These premiums are inexpensive, useful gifts, offered on the first call. One type of this premium is the "advance" given to a customer on the first call with the understanding that she'll buy a certain amount over a period of time to "trade out" the premium.

• *Club plans* are essentially mail-order businesses in which one woman is enlisted as a "secretary" to sell merchandise from a catalog to ten or more friends who pay a small weekly sum for their purchases. Premiums are given for each $10

purchase and are usually valued around $1 to $1.25 for a single $10 order, two or three times this amount for double- and triple-purchase units. This technique is widely used as a fund-raising device for clubs and religious and charitable groups.

Advice Available

For the company that wants to move into producing premiums, expert advice is available from the National Premium Sales Executives. NPSE, founded in 1956 by premium-supplier executives, devotes itself to the supplier's problems and needs "as they affect his value to the premium user." Twice a year, NPSE holds premium shows; the organization periodically disseminates information about the premium field; and research projects by an NPSE committee provide information on premium-sales potentials. The group has a speakers' bureau, and a public-relations program—aimed primarily at the business field but also touching the consumer—also has been established.

Suppose a manufacturer of a consumer product wants to run his first premium offer. Where does he start? Today, many suppliers can provide the user with help in setting up a suitable plan. Such suppliers will arrange a complete program for merchandising a premium and will aid in selecting the premium most suitable to the manufacturer's needs. Some advertising agencies have experts who specialize in buying premiums; these men are responsible for finding a suitable premium at the best price to fit the client's promotional requirements, and often they assume responsibility for developing the entire program.

Premiums often are used to help a company get off the ground. For example, California Oil Co.'s Chevron gasoline decided recently to use a premium to draw motorists into its stations. It chose a Kodak Brownie Bullet camera worth $4.25; the camera was offered to motorists for $2.25 plus a free coupon available at Chevron stations in the East. The camera proved successful for several reasons: It represented a bargain, it featured a camera name well known to everyone, and the promotion was scheduled at a time when people were taking to the road on vacations. The company made the premium do double duty: It promoted the premium with a push on television and in magazines and, to wrap up potential customers, it mailed a coupon to each of its credit-card holders.

Getting Started

What should be the first step in developing a premium-incentive program? One executive—C. W. Hellberg, president of General Consumer Products Inc.—suggests that a company should recognize that any premium-incentive merchandising program costs money; that such costs are legitimate and necessary

selling expenses; and that they should be so budgeted. "Start with the premise that premium merchandising is just a sales tool that costs money," he says. "The simplest way to budget such premium expense is to base it on a definite percentage of sales, credited to a reserve against which the expenses incurred will be charged. This procedure will provide a simple, easy-to-handle check-control formula."

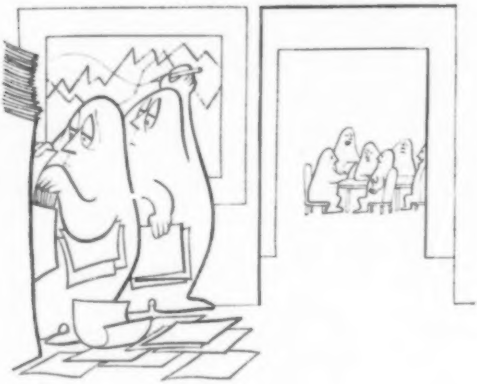
Next, Mr. Hellberg suggests, "you should make spot market tests—at least one and preferably several, if your distribution covers a wide geographical area. Such a test will tell you whether your idea is good, mediocre, or poor; where it should be altered; and whether the idea will produce the desired results at a cost within your budget. Your market test will either justify the costs of your plan or, perhaps, save you thousands of dollars by eliminating a plan you've found won't work." ♦

The Shift in Consumer Buying Habits

A DRAMATIC CHANGE is taking place in the way the consumer spends his money, reports Richard E. Mooney in *The New York Times.* The average American spending a dollar in 1953 spent 65 cents of it for goods and 35 cents for services. In 1960, the share for goods had declined to 60 cents and the share for services had risen to 40 cents. The shift of just one nickel per dollar adds up to more than 16 billion dollars more for services (and less for goods) for all consumer spending last year.

The total of consumer expenditures has risen enormously in the eight years, from 233 billion dollars in 1953 to 329 billions last year. Thus the fact that a declining share of the total is being spent for a given item does not mean that sales of that item are down. Food, for example, is the biggest single item in the consumer budget. Its share of consumer spending is down the most—from 28 cents a dollar in 1953 to 24 cents in 1960. But total expenditures for food rose in that time from 65 billion dollars to 80 billion dollars.

One explanation for the shift is that people are making, and spending, more money. When a consumer has met his primary needs, he has more left to spend in other ways. Changing tastes or ways of life provide another explanation. Persons with rising incomes frequently pay to have more services performed for them. They take more trips and they buy more on the installment plan. Also, housing is counted as a "service" here. Its share of consumer spending has risen with the rise in living conditions.



Plotting Future Manpower Requirements

Condensed from Employee Relations Bulletin

CORPORATE GROWTH over the past decade has been accompanied by a rapid increase in the ratio of supervisory and professional employees to the total work force, and the next ten years will see an acceleration of this trend. Thus manpower planning is a must for companies that don't want to be caught short in the 60's and 70's.

There are two methods of estimating future manpower requirements which, in the long run, can save a company thousands of dollars and millions of headaches. One is called "trend projection"; the other, "man by man" or "job by job."

In "trend projection," information is assembled on retirement, separation, promotion, and sales over the past several years. From these data, key ratios can be worked out, such as sales per employee. Projected sales, taken from the forecast budget, can then be used to determine future manpower needs.

In the "man by man" or "job by job" method, a supervisor or department head examines each employee in terms of retirement, promotion,

Employee Relations Bulletin (September 27, 1961),

and separation. Then he looks into each existing job and anticipates new requirements. From this he estimates specific manpower needs of each job to be filled.

A survey of six progressive companies shows how they are planning for the future. Minnesota Mining & Manufacturing Co. (St. Paul), for example, places heavy emphasis on the trend-projection method. Projections of future needs are made in specific job categories based on studies of manpower-sales relationships. Studies, started on the management level, have been expanded to include laboratory and sales personnel.

Projections are made for a five-year period and are reviewed as often as every six months. MMM has found its greatest shortage in the technical, sales, and management areas. To supply its needs, the company relies on a world-wide recruiting program that operates at every level of employment; three full-time recruiters implement the program.

Job-by-Job Method

Future requirements can be determined easily from past experience at Columbia Gas (Charleston, W. Va.). Using the job-by-job method, the company employs a Personnel Development Chart that shows what is happening (promotions, transfers, retirements) to each employee. Once a year, every department submits to the personnel department recommendations for future hiring plus suggestions regarding specific job categories projected for a year in advance. Employees are also recommended for advancement and for participation in the company's training program.

Columbia's policy is promotion from within; to facilitate this, new employees are not assigned to permanent jobs but are rotated systematically for the first few years to broaden their background.

Annual Planning

Itek Corp. (Lexington, Mass.) finds that manpower-planning techniques work best on a fiscal-year basis. The company has grown so rapidly through mergers and acquisitions that longer-range forecasting is not practical. Recommendations covering every level of employee are made to Personnel by each department.

Technicians — principally engineers and physicists—make up the greatest shortage in the forecast. Itek is attempting to fill these expected shortages by advertising in technical bulletins and employment agencies. Some 95 per cent of their new employees come from other companies—mainly through want ads.

Five-year projections of manpower requirements are made by International Business Machines Corp. (New York, N. Y.) at its central headquarters. These cover only major categories. Each division pre-

pares its own figures on more detailed breakdowns. Predictions do not go beyond five years since they must be based on sales trends and, says R. A. Whitehorne, Manager of Employment and Education, these are unreliable over a longer period.

Trend Projection

Sylvania Electric Products, Inc. (New York, N. Y.) has shifted from forecasting for the entire company to divisional forecasting. To do this, it uses trend projection. Net sales for several previous years are divided by the number of employees; results are then compared with sales expected during the next five years. In addition, each supervisor plans on a "man by man" and "job by job" basis.

Sylvania also prepares charts that project the net growth and loss of personnel in various categories; show the changing relationship of salaried to hourly employees; show the company-wide separation and quit rates; and show the change in the number of managerial personnel, both by separation and hiring. Rapid expansion makes Sylvania dependent on experienced personnel from other companies rather than on college trainees. But in critical areas, outside personnel are hired only if an intensive search fails to turn up a promotable employee.

The Port of New York Authority (New York, N. Y.) analyzes its past manpower requirements and compares its turnover figures with the national manufacturing average and federal statistics. The Port Authority also prepares separate reports on fifteen other companies in the New York area, projecting its figures and theirs over a five-year period. These figures are then analyzed for trends which can be translated into future manpower needs.

The budget forecast, indicating anticipated staff changes by each unit, is another source of information. The reports are submitted each September for the following year. The agency also prepares a long-range, ten-year personnel forecast based on predicted population growth of the community, sales forecast, and technological conditions. The greatest shortage facing the agency is that of highly skilled mechanics. To offset this—and to avoid hiring scarce mechanics at premium pay from other organizations—the Port Authority has developed an apprentice program, recruiting high school students.

Possible Steps

Every company can take certain steps to assure an adequate supply of scarce manpower:

- Obtain sales forecasts of the next few years and translate them into the need for additional employees by job category.
- Maintain an accurate forecast of the company's retirement rate.
- Exchange data with other personnel executives in the area.

• Consult the Department of Commerce for basic figures on growth in your industry; consult the Department of Labor's *Occupational Outlook Quarterly* for trends within job classifications.

• Check your current ratio of professional, managerial, and technical staffs to total employment against your 1956 figure. If it has increased, you may have to plan for greater increases in the future.

• Estimate carefully organizational changes over the next five years. Automation or electronic data-processing, for example, could drastically alter your manpower mix.

• Fill manpower gaps as soon as possible by training current employees or hiring new ones. ♦

Room at the Top

ONE DAY recently, the Sun Shipbuilding and Dry Dock Co. went through a simple ceremony that will be repeated in scores of companies in the coming year. Sun's President Richard L. Burke was retiring after eleven years at the helm of the big Chester, Pa., shipyard. In his place came forty-year-old Paul E. Atkinson, who had started at Sun as a shipfitter's helper in the early 1940's.

Seemingly a routine incident, Sun's changing of the corporate guard holds explosive implications for executives on all levels of management, writes Jack J. Friedman in *Dun's Review and Modern Industry*. For, as a result of an increasing accent on youth, the cliché about "room at the top" is becoming more of a reality each day.

The opportunities ahead are clear from a study of the hundred largest corporations in America today. The study indicates that the upper echelons of all these companies are fast reaching 65, the age at which the average corporation executive retires. Among the study's findings:

• Just four years from now, the hundred corporations will need sixty new vice-presidents to fill the offices vacated by men who have reached the retirement age of 65.

• Two years later, 1967, may well become known as the best year in history for executive opportunity, with no less than 14 per cent of those same companies combing their ranks for new presidents.

• Far more difficult to chart, a possible trend to younger board chairmen could mean seven openings among the hundred chairmanships jobs in 1965.

Are these figures too optimistic? If they err, surprisingly, it is probably on the conservative side. Computed on a man-for-man basis with relatively minor projections, they consider only the positions now existing in business; they make no provision for the increasing specialization, technological developments, and expansion that are bound to create new executive positions, the writer notes.

EQUIPMENT RENTAL—

When Does It Pay?

Condensed from Factory

RENTING CAPITAL EQUIPMENT is now a familiar custom in many companies. The reasons for using rented equipment are many, but three of them are becoming increasingly important to operating management: improved maintenance, maximum use of equipment, and elimination of idle equipment.

A properly devised long-term rental program normally includes these arrangements:

- All obligations pertaining to the equipment—maintenance, servicing, replacement, insurance, etc.—are assumed by the renting company.

- Rates are based on the lessee's past experience, not on competitive quotes. If the renting company finds that a lessee's utilization rate is higher than normal, it will charge a higher rate for the rented equipment.

- A thorough survey of the lessee's relevant operations will be made by the renting company, with an eye to improving efficiency of the over-all operation. The best equipment for the lessee's needs will be recommended. In some cases, the renting company will buy the manufacturer's existing equipment at current fair-market prices. It may be replaced with new and better equipment, or it may be rebuilt and rented back.

- The rental agreement will be written as a true rental plan from the viewpoint of the Internal Revenue Department, so that it may be allowed as a deductible expense.

When maintenance is handled by the lessor, a manufacturer's internal maintenance force usually can be reduced. One company, for example, had spent $23,000 per year maintaining seventeen lift trucks extending in age from one to thirteen years. By renting fourteen new trucks in place of the old ones (which were bought for their residual value of $20,000), the plant obtained a single tax-deductible budget figure of $2,496 per month. The rented trucks are newer and better; all maintenance is done by

the renting company; and the plant maintenance force was reduced by two men.

Operating managers, of course, have found other benefits from renting capital equipment. Consider lift trucks again. Space formerly used for truck maintenance can be used for production. No spare parts need be carried; there is no loss from their pilferage or obsolescence. (One plant surveyed by a renting company found $20,000 in obsolete parts for trucks no longer manufactured.) Scheduling can be based on uninterrupted work: If the trucks break down, they will be replaced—provided, of course, that the renting company has an adequate stock of replacement equipment.

Another advantage to operating managers in renting some types of capital equipment lies in paying for only the minimum number of units needed for average production. Seasonal peaks or emergencies can be handled with short-term rentals at special rates from the same lessor. This eliminates depreciation, insurance, storage, etc. for surplus equipment not used during slack periods.

Equipment rental also produces fringe benefits: more accurate budgeting of future costs, tax benefits (if the contract is properly executed), and a hedge against inflation.

How Much Does It Cost?

To find out whether the costs of renting capital equipment are more or less than present equipment expenses, take these four steps:

- Determine the number of years you want to rent. This figure is usually based on the optimum economic life of equipment.
- Decide how many units of equipment will be retained and how many will be replaced.
- Study past costs of equipment. Use this as basis for projecting their future costs under company ownership.
- Compare final projected costs with the arrangement offered by the rental company.

When computing cost projection under company ownership, be sure to include these factors:

- Cost of equipment and accessories, transportation charges, sales taxes, etc. (less residual at the end of the term).
- Cost of capital, including all interest (or financing charges) on capital tied up in equipment.
- Maintenance costs. If you maintain a repair shop, include all direct and indirect shop costs such as payroll costs, rent, light, heat and power, depreciation of shop equipment, tools, insurance, record keeping, etc. If you do not have a repair shop, include charges for outside service calls, parts, preventive maintenance, emergency calls, and overhauls. All costs, compiled from your records for past years, should be adjusted to current price levels.
- Cost of insurance, including fire and theft.

• Taxes, including personal property, excise, and use.

• Other overhead costs, including those of the purchasing department. (This is to include time costs of interviewing salesmen, evaluating equipment, issuing purchase orders, keeping records, etc. The average cost of processing and receiving orders for maintenance parts was found in a recent survey to be not less than twenty dollars an order.)

Include, too, costs of the receiving department (including costs of checking replacement parts received, preparing receiving reports, following up material, etc.); storage expenses (including costs of receiving parts and supplies, stocking and issuing parts, physical inventorying, record keeping, etc.); accounting department expenses (including cost of checking invoices, posting books, preparing accounts payable); and management time.

• Losses from down time. Include losses from idle personnel, production stoppages, shipping delays, costs of renting substitute equipment on short term, and cost of owning and maintaining stand-by equipment. (According to one survey of representative industrial plants, the cost of unscheduled down time averages $16.28 per hour.)

• Losses from rising costs, covering estimated increases in price levels for labor, parts, and overhead. (Hourly labor rates for "All Manufacturing," according to the Bureau of Labor Statistics, have increased at an average of better than 5 per cent annually over the past several years. Similar rates of increase have been experienced for the cost of parts, supplies, fringe benefits, and other overhead items.)

• Obsolescence (including that of parts) for existing equipment to be continued in operation.

• Profits lost by capital tied up in equipment. Additional profits to be earned by investing funds freed by renting in the production of the company product can be computed by this formula: Funds tied up in equipment times annual turnover rate of capital times annual profit ratio equals extra profits to be earned.

When making your comparison, don't forget to adjust factors to current price levels, and give full consideration to inflationary aspects of prices in the future: You are comparing what costs will be, not what they are today.

To obtain a rental quote for comparison with your own costs, contract a reputable company. One that knows its business will develop a contract price for your needs—but only after a thorough analysis of your plant's operation. They will look at your running hours of equipment, maintenance requirements, equipment needs, and optimum number of units needed for your operation. They might also submit suggestions for revising present production patterns. ♦

The Pros and Cons of EXECUTIVE STOCK OPTIONS

■ **Richard C. Smyth**
President,
Smyth & Murphy Associates, Inc.

THE PAST YEAR has seen a sharp rise in the drumfire of attacks on one of management's most highly regarded methods of executive incentive payments—the stock option. Critics have claimed that stock options are designed to enrich already highly paid executives at the expense of the company's stockholders. They have called them unjustifiable tax dodges; they have claimed that they contribute to inflation; and they have accused options of tending to discourage competition and hence of restricting the growth of the economy. Such criticisms as these have been appearing with increasing frequency in the business press, and they are even beginning to turn up in such popular publications as *The Saturday Evening Post.*

The target of this barrage is a comparatively recent arrival on the compensation scene: restricted stock-option plans. These are plans by which a company can give se-

A MANAGEMENT REVIEW SPECIAL FEATURE

lected executives an option to purchase a stated number of shares of the corporation's stock for a sum not less than 85 per cent of its current market price. (In practice, many companies set the option price at 100 per cent of the current market.)

During the past decade, there has been a phenomenal increase in the number of companies using stock options. In 1953, *Business Week* reported that about 30 per cent of the major companies in the country had stock-option plans; today, an analysis of 360 of the largest U.S. industrial companies indicates that 73 per cent of them are using stock options as one means of compensating and motivating their executives.

How Executives Benefit

The advantage of a stock option to an executive is obvious. Say, for example, that a man is given an option to purchase 1000 shares of his firm's stock at 100 per cent of its current market price of $100 per share. Assume that this option may be exercised at the end of two years. If, at that time, the stock's price has remained the same or declined, the option is obviously worthless; but if the price of the stock has increased—say to $150 per share—the executive has something of value. He may exercise his option and purchase the thousand shares at $100—receiving, in effect, an incentive bonus of $50,000 worth of stock. After six months, he may dispose of his stock and pay only a capital gains tax on the $50,000, rather than the higher rate that would apply if it had been paid to him directly as compensation.

Loss of Revenue

The fact that gains under a restricted stock option, when they meet the holding requirements of the tax code, are taxed at the long-term capital gains rate—a maximum of 25 per cent—is frequently cited as the cause of a substantial loss of revenue to the government, and it is sometimes referred to as a "tax loophole." United States Senator Albert A. Gore has estimated that this tax loss is as high as 100 million dollars a year.

Dean Erwin N. Griswold of the Harvard Law School believes that any profit arising from the spread between the option price and the market value when the option is exercised should not be classed as a capital gain at all, because an essential element of capital-gains transactions—risk—is missing. This element of risk, he says, is one of the chief reasons for taxing capital gains at a special rate.

Proponents of stock-option plans, on the other hand, question whether there is in fact any appreciable loss of tax revenue—or, indeed, any loss at all. Writing in *Harvard Business Review*, Henry Ford II has pointed out that the company must give up a tax deduction of 52 cents

"Closing so-called tax loopholes is not the answer to our federal tax problems . . . What is really needed is a thoroughgoing, objective review of the entire tax code, with a view to eliminating its basic inequities . . ."

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on each dollar of incentive provided in this way, rather than as salary or other means of compensation. If the optionee sells his stock, he must pay an additional 25 cents on each dollar in capital-gains tax—and, if he holds the stock until he dies to avoid this tax, his gain is still subject to the estate tax.

Growth Generates Taxes

Moreover, it has been pointed out that stock options are designed to be incentives to increase corporate profitability. To the extent that they do, additional tax revenues are produced—and these are quite likely to exceed any revenue that may be lost as a result of the preferred tax status of option plans.

It is obvious that all these factors were considered by the Congress when the tax code was amended in 1954. Closing so-called "tax loopholes" is not the answer to our federal tax problems; one man's loophole may be another man's lifesaver. What is really needed is a thoroughgoing, objective review of the entire tax code, with a view to eliminating its basic inequities—including the confiscatory ordinary income tax rates at the higher income levels.

Options and Inflation

A viewpoint prevailing in some economic circles—one that is reflected in the report of the Senate Subcommittee on Antitrust and Monopoly in 1957—is that stock options have the practical effect of feeding inflation. The reasoning is that the stock options given to executives connect their income and wealth to the market value of common stock. Since price increases tend to raise stock prices, the financial interests of executives are advanced by rising prices of the company's products. This reasoning implies that executives will raise prices unreasonably and unnecessarily in order to increase first their company's profits and ultimately the market price of their company's stock in order to make their options more valuable.

There are major fallacies to this line of reasoning. For one thing, it overlooks the fact that corporate profits (and hence stock prices)

may be increased by other methods than by price rises—by reducing costs, by marketing new products, or by increasing sales volume, to name only a few.

Moreover, even executives who would like to raise prices to further their own interests would find it more easily said than done. The critics who advance this argument ignore completely the restraining effects of competition, both in this country and abroad; it doesn't take too much knowledge of today's competitive marketplace to realize that arbitrary price rises are a luxury that few if any companies can afford.

Not only would domestic competitors welcome the opportunity to win a larger share of the market for themselves, but foreign companies would be only too happy to widen their foothold in many markets. The rebuilt economies of Japan and Western Europe now have manufacturing techniques and equipment and facilities as modern and advanced as any in this country, and in many product areas—including instruments, electronics, clothing, and machinery—they are able to

"So that's what Benton meant by a second income."

import and sell goods at a price less than the cost of manufacturing a comparable product in this country. Faced with this kind of competition, a company would be rash indeed to think that it could increase its profitability by raising the prices of its products.

Restricting Competition

Senator Gore and others have also claimed that the use of stock options discourages the vigorous growth of new and smaller companies, which might pose a challenge to the Big Three's and Big Four's of so many industry groups. To the extent that corporations are able to hold their executives by means of stock options, management tends to remain with large and well-established concerns, rather than leaving to set up competing companies. Thus, these critics complain, stock options serve to encourage oligopolies and monopolistic practices.

An allegation of this type is almost impossible to prove or disprove. However, we do know that our economy is the largest, most complex, and most varied in the world. It is continually growing, and it continually offers a plethora of new goods and services. Whether or not the rate of growth of the economy is fast enough is debatable, but it is difficult to believe that stock options have had a detrimental effect on the over-all growth rate.

It is true that stock options are an incentive for executives to remain with their companies, but it is doubtful that any business units they might have created if they had left their companies are forever "lost." There are many capable and enterprising people who are willing and eager to take advantage of any unfilled need or economic opportunity that might arise.

Options and Other Stockholders

One of the most frequent charges is that stock options dilute the equity of the shareholders and are unfair because the executive is permitted to buy stock at a much lower price than other stockholders. Senator Gore has called stock options "cut-rate bargain purchases for highly compensated executives," and Dean Griswold has referred to stock options as a "heads I win, tails you lose type of lottery."

Unfortunately, emotional phrases seldom illuminate economic problems. It is perfectly true that the executive optionee can buy stock for less than the typical shareholder in his company, and that some dilution of equity results when the executive exercises his option. However, let us examine the full extent of this dilution and the *quid pro quo* that is also involved.

A Case in Point

Assume that the executive has an option on a designated number of shares of stock at an option price of 95 per cent of the fair market value of the stock at the time of the

option grant. The true cost of the option is not the spread between 95 per cent and 100 per cent, but the spread between 95 per cent and the market price of the stock when the option is finally exercised. Based on the length of the average option and stock price trends over the past decade, this will amount to about 50 per cent in the average case.

Dilution of Equity

Assume that a company has one million shares of outstanding common stock, and that the current market price is $100 a share. Studies have indicated that the average stock-option plan utilizes 6.2 per cent of the company's authorized and outstanding common shares for option purposes. Assume, then, that 95 per cent restricted stock options have just been granted to the company's executives on 62,000 shares—6.2 per cent of the authorized and outstanding common stock. Assume further that five years from now the market price of that stock is $150 a share, and that all the options are exercised in full at that time.

In these circumstances, the company will receive $5,890,000 for the 62,000 shares of option stock. Since the stock is then selling for $150 a share, the company should theoretically have received $9,300,000 for the stock if it had been sold on the market, or $3,410,000 more than was actually received. Thus, the actual dilution of equity in this hypothetical case is about 2.3 per cent of the theoretical value of the one million shares outstanding.

The Quid Pro Quo

In exchange for this theoretical 2.3 per cent loss, however, the shareholders have secured two very tangible benefits: (1) the services of the executive group for five years, and (2) a 50 per cent increase in the value of the shares each stockholder holds. It is indeed difficult to see how the stockholder has suffered any loss. In fact, in hundreds of companies, shareholders have voted overwhelmingly in support of stock-option plans, hoping that they would benefit to the same extent as the stockholders in the hypothetical but typical case that has been outlined above.

It is sometimes forgotten that unless the company granting the options prospers, the options have no economic value to executives. In May, 1957, for example, the Pennsylvania Railroad granted options at $21 a share to approximately eighty officers and executives of the railroad. As of now, the options have no value to the optionees, since the stock is selling at about $15 a share—and they will never have any value unless management can reverse the railroad's fortunes and substantially increase the price of the stock. If they should succeed, it would be a rare stockholder who

"Actually, stock-option plans are so prevalent today that most companies in most industries must have them in order to be competitive in an increasingly tight management labor market . . ."

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would begrudge management's sharing in the fruits of the success.

Holding Competent Managers

Why are more and more companies adopting stock-option plans for their executive personnel? Simply because stock options offer advantages that many companies find they cannot afford to overlook.

First of all is the assistance that stock options provide in attracting and retaining competent management personnel. More than any other single factor, the quality of its management will determine whether a company succeeds or fails over the long pull. Good executives are hard to find and train—and they are easy to lose, particularly in periods of business expansion, when the general shortage of competent executives becomes more acute.

Stock-option plans, if properly designed, tend both to attract and to retain executives. Testifying before the Securities and Exchange Commission, Gwylim Price, chairman of the board of Westinghouse Electric Corporation, noted that three Westinghouse executives had turned down presidencies of well-established, nationally known companies because they had Westinghouse stock options.

Actually, stock-option plans are so prevalent today that most companies in most industries must have them in order to be competitive in an increasingly tight management labor market.

Motivating Executives

Stock-option plans are also a powerful factor in motivating management to achieve corporate growth and profitability objectives. In the early days of modern business, ownership and management were synonymous. Today, however, ownership is usually dispersed widely through stock ownership, and in some companies the executives own none of the stock.

It is generally true, however, that stockholder interests are better protected when executives have proprietary interests, through options or ownership of stock in the company. This provides an added incentive to produce profits and achieve corporate growth, and to

consider the long-range aspects and implications of current decisions.

Many companies have found this to be true. A few years ago, for example, a special committee of outside members of the board of directors of the General Motors Corporation made an analysis of the corporation's management-incentive program. In its report, the committee said in part, "Substantial stock ownership by its management is an important factor in the success of any enterprise. The relatively large stockholdings in General Motors Corporation by its executives have played an important role in bringing the corporation to its position of industrial leadership."

When Decisions Count

Stock options are extremely advantageous in business situations where long-term corporate growth and profits depend more on executive decisions and actions than on general business cycles. This is especially true in companies where technological advances are vital for success, such as in the electronics, petrochemical, or drug industries, and in companies where style trends significantly affect sales, such as in the automotive or clothing industries.

It is also true of young companies or companies in difficulty that are being revitalized. Companies in these categories are seldom able to offer the cash rewards that would be needed to attract executive talent, but an executive may be willing to join the firm and sell his services for a relatively small current salary plus an option to buy stock. In 1932, for example, Remington Rand Company made such an arrangement with James H. Rand, at a time when the company was losing money and its stock was selling at $1.50 a share. Mr. Rand was given an option to buy 100,000 shares at ten dollars a share. Five years later, he exercised his option when the stock was selling at $28.50 a share.

The Case for Options

Restricted stock options are both legal and ethical means of compensating and motivating members of management in business and industry in this country. As competent managers build larger and more successful companies, their options will assume meaningful value—and, at the same time, the shareholders will benefit as their shares appreciate in value. Finally, all society will benefit, because profitable companies both provide stable jobs and security for their employees and create new jobs through corporate growth and the development of new and improved products and services. ♦

ECONOMY has frequently nothing whatever to do with the amount of money being spent, but with the wisdom used in spending it.

—Henry Ford

Marketing Roads to Ruin

By D. F. Houlihan

Condensed from The Price Waterhouse Review

MARKETING MANAGEMENT can contribute substantially to the profitability of company operations. But in order to reach this goal, marketers must beware of wandering down tempting but disastrous roads to ruin.

One such road involves an overemphasis on volume, coupled with a misuse of marginal pricing. It is true that increased volume produces increased profits—provided that the cost of getting this volume does not exceed the profit it brings. The danger starts when we consider two courses of action:

- Building volume by setting prices so that different groups of customers or different products bear disproportionate shares of the cost.
- Setting some prices so that we cover our direct cost but not our full costs—thereby making not a true profit but a "contribution to overhead."

Under this concept, we determine those direct, "out-of-pocket" costs which vary proportionately with volume. We treat these costs as a basic figure; any recovery in sales prices in excess of this figure represents a marginal contribution. This contribution is supposed to pay all of our fixed costs, such as supervision, depreciation, insurance, and taxes; to pay the costs of marketing and distribution; and to provide us with a profit.

Those who overemphasize volume tell us that if we can attain sales over and above those we would normally expect, and can make them at prices which exceed the direct costs and contribute something to our marginal income, we are providing a benefit for the company by increasing its profits; we are gaining volume. However, they neglect to tell us who is supposed to pay for the overhead, marketing, distribution, and the profit that should exist at a normally anticipated volume.

Once we start cutting sales prices, a variation of Gresham's law begins to work: "Bad prices drive out good." Unless we can so restrict the

impact of "bad" or marginal prices that they will not affect the bulk of our business, a new and lower price level almost certainly will result—for all sales.

A Useful Concept

Marginal pricing can, of course, be useful. For example, one company, during a temporary recession, employed the principle of direct costing, or covering its out-of-pocket expenses, to obtain a new, relatively large account. In going after this business, the company took into account three points: (1) Due to the nature of the business, which involved a high degree of service, it would be difficult for another company to take the account away from them once the customer had been satisfied; (2) the recession would be temporary; and (3) the improvement in general business conditions would support an increase in price over the long term which the customer would be willing to pay. Fortunately for this company, all the factors upon which the original low price bid was made worked out, and the customer is now paying what might be considered reasonable trade prices.

In many cases—for example, where a company wishes to break into a new territory, introduce a new product, or perhaps make a bid on a large contract—management is wise to determine the direct cost of the products to be sold. By adding to this cost the expenses of marketing, distribution, and administration, management will know the "out-of-pocket" break-even point of such products. Although it might be good business to make certain sales on this basis, the company should price the remaining sales high enough to cover overhead and their share of marketing, distributing and administrative expenses, and profit.

The Full Line

Another road offers "the full line and national distribution" as a sure path to profit. One of its bypaths is the "loss leader," and following it can be a dangerous policy. The "loss leader" can well become the major product because it becomes so easy to sell and so good to buy; customers might disregard the rest of the line.

Many companies today are reappraising their marketing policies and pricing policies to eliminate the loss leader and to make each product stand on its own feet. Similarly, many distributor organizations are analyzing profitability of operations by product line and are reassessing the relationship between customer service and carrying a full line. Products that do not pay their own way on a net-profit basis are being discontinued—usually with the advice and assistance of the manufacturer, who realizes that the distributor must have a profitable operation if he is to stay in business.

A third detour is the belief that it is necessary to take all orders,

large or small, and to call on all customers every week or oftener—"to make sure we get all the business." Wise marketers, however, have learned the "80-20 rule": 80 per cent of the sales volume will consist of 20 per cent of the items; 80 per cent of the sales will come from 20 per cent of the customers; 80 per cent of the inventory will be in 20 per cent of the items. This generality—which applies in many activities of industry—raises several questions. If 80 per cent of our customers provide only 20 per cent of our sales, what are we doing to minimize the cost of carrying on business with these small customers? Do our salesmen call on these small customers as often as they call on large customers?

When Costs Exceed Profits

One company provides an interesting example of this problem. In establishing pricing schedules, the company set a price of $2 per thousand for a certain item for sales in quantities up to 20,000. A study of the costs of this company disclosed that there was a fixed cost of $8 an order just to receive the order, write the acknowledgment, schedule the production, make the billing, and collect the account. Considering all production and administrative costs, the company computed that no sale of $40 or less could be profitable; yet a substantial number of the orders for this product were for quantities of 5000 to 15,000. Here was an activity which was costing more to carry out than could possibly be received in gross profit on these orders. Disclosure of these costs and discussion of the problems with sales management led to a revision in sales emphasis and in pricing policy.

Informed Decisions

To avoid the roads to ruin, sales management must be in a position to make informed decisions. It must have information such as the following:

- How many calls do salesmen make in each territory, to each customer? How much does each call cost, including salaries, expenses, car allowances, and the like?
- How much business are we getting from specific customers or groups of customers as a result of these calls, and what size are the orders?
- What does it cost to reach various groups of customers through promotional and advertising activities?
- How much does it cost to receive an order, schedule it, ship it, bill it, and collect the receivable?
- What is the minimum size order in various product classes which can be profitable, considering the foregoing fixed costs of doing business?
- In view of the costs disclosed by these studies, how adequate is our pricing policy for various order sizes? ♦

Profit-Sharing—a Competitive Weapon?

By Peter F. Drucker

Condensed from The New York Times Magazine

PROFIT-SHARING is in the news again. The recent agreement between the American Motors Company and the United Automobile Workers has put profit-sharing into an important labor contract for the first time.

News of the contract has produced many violent reactions. The "true believers" in profit-sharing, for whom the concept is the infallible remedy for every ill of industrial society, have hailed the agreement as bringing the dawn of a new era; others immediately denounced it as a "giveaway," a "betrayal of the stockholder," and an "abdication of management."

What are the facts about profit-sharing? How does it work? What does its accomplish? First, profit-sharing is neither a specific thing nor a specific plan. It is a financial tool that is being used in totally different ways for different purposes and different beneficiaries. The only

The New York Times Magazine (October 15, 1961).

features these different uses have in common are accounting and tax formalities.

There are three kinds of profit-sharing plans: the almost extinct plan for giving extra worker pay out of a share in profit; the luxuriantly growing executive-pension plan financed out of profits; and the modestly prospering plan that finances standard employee benefits out of a share in the profits.

Easing the Burden

The significant profit-sharing plans in use today—including those of Sears, Roebuck, Procter & Gamble, and the First National Bank of Chicago—number no more than three or four hundred. But they cover the most employees: 1.5 million out of the total of two million employees under all forms of profit-sharing, with the Sears plan alone accounting for 150,000 people.

Essentially, these plans are designed to ease the burden of employee benefits on a company's earnings and cash position by having that burden fluctuate with profits. Benefits in the majority of these plans are as fixed as in many of the standard plans for retirement pay, group life insurance, or hospital insurance. Although the employer's payments—the insurance premiums for these benefits—are flexible, they must, of course, average out over the years to the same amount that a non-profit-sharing plan with the same benefits requires.

Such plans have not created much excitement among the proponents of profit-sharing: Their aim is too modest and their growth too slow and limited. In the few cases where such a plan has had spectacular results, the reason has been some feature other than profit-sharing. The Sears, Roebuck plan, for instance, is successful not merely because each employee gets a share of the profits but because the company has been investing these profit shares in its own stock—and it has been a very successful company over the years. If some other less successful enterprise had followed the same practice, there would be little today for an employee to retire on. However successful Sears has been, therefore, most managements and union leaders have declined to follow its example.

Modest Goals

In the great majority of these profit-sharing benefit plans, both goals and results are modest and unspectacular. For example, the employee handbook of Champion Papers, Hamilton, Ohio, describes its profit-sharing plan as follows:

"Profits vary. They can be up one year and down the next, so it isn't practical to tie current pay—'money for today'—to profit. The idea is to use Champion's profit to provide 'money for tomorrow'—the insurance and retirement and other benefits for Champion employees and their families . . . So we accu-

mulate this 'money for tomorrow' out of profit—putting in more when profit is up, less when it is down. That way, we should be able to provide more money than if we had to put in a fixed amount every year...."

Viewed purely financially, the American Motors plan does not differ significantly from the Champion Paper plan or from that of a number of oil companies, banks, insurance companies, or retail chains. The only difference is interesting rather than important: The American Motors plan is, to some degree, a "profit-and-loss-sharing" rather than a straight profit-sharing plan. In a poor year, the difference between the amount available from earnings and the payments needed for the promised benefits is to be raised by cutting back the contractual annual wage increase.

Ambitious Aims

However, the aims of the two plans are quite different. American Motors' first aim is to resolve the conflict between two equally important needs of our economy: to remain able to compete in an increasingly competitive world, and to remain a high-wage society with constantly rising standards of living, especially for the lower-income groups. The plan's second aim is to find a new approach to labor relations that establishes a community of interest between the company and its employees.

American Motors hopes to achieve its plan's first aim—that of making a high-wage economy truly competitive—by making all future increases in employee benefits a charge against profits rather than a fixed cost-per-hours-worked. It is this intention to make additional benefits henceforth dependent on company earnings that makes the plan a labor-relations novelty.

Recovering Costs

American Motors' President George Romney underscored this aim in the announcement of the contract this summer. He pointed out that a charge against earnings does not have to be included in the cost base which determines prices. This might mean that a company that now breaks even when it sells 100,000 units at a given price can, under the new approach, recover its costs with sales of 90,000 units at the same price, or with sales of 100,000 units at a price 5 per cent lower. If it follows the first path, it will have fewer loss years; if it follows the second path, it will be able to compete much more successfully.

The importance of this lies in the impact of benefits on U.S. industrial costs. For every dollar paid out in wages, the typical manufacturing company pays out twenty cents or so in fringe benefits—from sick pay to scholarships for employees' children. If all this were to become a charge against earnings rather than part of the cost structure, prices could be

lowered about 10 per cent. And even our lowest-cost competitors, such as West Germany or Japan, do not by and large have that much of a cost advantage.

The other aim of the plan—a "breakthrough in labor relations"—is something the company's management has long called for. But it was Walter Reuther, president of the UAW, who emphasized this point in the public announcement of the agreement when he spoke of the "breakdown of collective bargaining in many industries" and of the futility of labor relations based upon the "power concept." This acknowledgment by Reuther of the need for new approaches to labor relations may be more significant than the American Motors plan itself. ♦

Companies Help Employees Acquire Stock

IT'S GETTING HARDER and harder to tell an employee from a stockholder, notes *Business Week*. About one-fifth of the companies listed on the New York Stock Exchange now have some sort of employee stock-acquisition plan, a new study by the Exchange shows, and more than 1.6 million employees (about half of those eligible) are participating.

Most of the 248 plans offered by 233 listed companies are for salaried employees, although hourly workers are sometimes included. Most popular with the employees are profit-sharing plans; they have had nearly a 100 per cent participation rate. In 23 of the 39 listed-company profit-sharing plans, employees make no contributions to the funds, which are invested in company stock and sometimes other securities. Under the other 16 plans, employees are either permitted or required to contribute up to 10 per cent of their salaries.

Most popular with the companies are stock-purchase plans, under which companies absorb fees but usually do not contribute toward the purchase price of the stock. There are 114 such plans among NYSE members, with 31 per cent of the eligible employees participating. They are particularly common among utility, petroleum, and natural-gas companies.

The 80 member-company savings and thrift plans (under which companies contribute from 25 cents to two dollars in common stock for every salary dollar set aside by the employee) cover the greatest number of employees—753,000. The participation rate is 76 per cent.

These three types of plans account for more than 90 per cent of the stock-acquisition schemes reported in the NYSE study. Other plans used include the Exchange Community's Monthly Investment Plan, stock-retirement plans, and stock-bonus plans. Plans for executives only were not included in the survey.

Organizing SERVICE and SUPPORT Groups

By Warren W. Wood

Condensed from Business Management

Every firm has creative, technical, or other specialists whose skills are used to support the more output-oriented departments. Examples are computer programmers in a decentralized office system, draftsmen or technical writers in an engineering company, and maintenance men in a plant. How a company organizes these specialists will determine how much they contribute to profits.

Generally, there are three basic ways to organize support groups.

Centralized Specialists

In the completely centralized pattern, all practitioners of the same specialty are brought together under a supervisor experienced in that skill. There are many advantages to this arrangement:

Control. Lines of control and communication are short, permitting adequate delegation and supervision of the specialists' duties. Specialists are evaluated as (and against) specialists; this simplifies decision-making concerning promotion, retention, and elimination. Estimates of time, cost, and manpower requirements are easily figured because performance records can be accumulated for such a group.

Economy. The centralized group provides for economy of effort. All companies have some irregularly scheduled tasks on which several days of hard work may be followed by several more days of waiting for checking, approval, and release. With a centralized organization, an experienced specialist-supervisor can assign a waiting specialist to another job, have him help someone else in the group, or put him on general administrative tasks. Thus a specialist's temporary free time can be profitably filled.

During a "crash" effort, the manager of a homogeneous group can assign people intelligently from less pressing to more pressing tasks. The "crash" finished, the specialists can return to their regular jobs, and no

staff reduction at all is necessary.

Flexibility. The homogeneous group is a readily usable tool in itself. If, for example, several draftsmen or writers were needed to help a particular section, the whole group could be assigned as a unit.

Decentralized Specialists

The opposite of the centralized, homogeneous grouping is the pattern where the specialists form no group at all but are scattered throughout the company, helping only the particular sections to which they "belong."

The main advantage of this pattern is that each specialist has an extremely high potential serviceability. Through daily exposure to the work going on in the group he serves, the specialist has an excellent opportunity to become expert in the specific subject material. Thus he becomes more independent and more competent to carry on without detailed direction.

On the other hand, there are a number of drawbacks to this organizational pattern. For example, since a specialist cannot be evaluated by the same standards that apply to the nontechnical members of the group, his professional advancement is always a special case. And, since the isolated specialist "belongs" to one group, he cannot be easily borrowed to help out elsewhere. Further, the isolated specialist receives no help, criticism, or instruction from experts in his field and cannot transmit his experience to others.

The third organizational pattern for the support group promises to correct the shortcomings in the other two patterns. Here the specialists are closely organized into a group under a specialist-supervisor in a single line of command, but perform their work in different sections of the company. In effect, they are farmed out, receiving general direction and personnel administration from their own supervisor and specific tasks from the supervisor they serve.

Combined Advantages

This pattern capitalizes on the same high technical expertness possible under the decentralized pattern, and adds the advantages of the homogeneous-group organization: evaluation, control, supervision, training, and flexibility. Other advantages are these:

Briefings. Regular briefing sessions can be held, where criticisms can be exchanged, problems ironed out, indication of new work evaluated, and deviations eliminated. This procedure offers great value in developing product consistency.

Supervision. Even though the specialists may be scattered about in various departments, proper supervision is still practicable. From his knowledge of his subordinates, an experienced specialist-supervisor can formulate standards for their performance that take into consideration periods of both good and

poor production. Marked deviations from these standards can be checked by examining the workloads in the departments the specialists serve, the behavior of the specialists themselves, and the work flow from inception to completion.

Training. Training continues systematically under this organization. New employees are sent along with more experienced ones to learn the ropes, and, since this training is highly individualized, a new employee can start producing sooner than he would if merely handed an assignment on a do-or-die basis.

Comparing Patterns

The completely centralized staff is probably the easiest to organize and control. Its supervisor and staff share common interests, backgrounds, and training; the functional homogeneity of the group facilitates its use when and where needed; and estimates and similar bookkeeping are simplified because accumulated performance records are available. It can comfortably house employees of both upper and lower grades of professional and technological skill because they are directed and evaluated in relation to each other instead of against a company-wide scale.

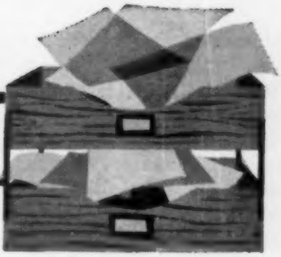
A manager might select this pattern when he has several people in the same specialty, when he wants to delegate their supervision, when he needs to be able to throw the entire group into a task with a minimum of dislocation, and when he is seeking reasonable economy.

Most Economical Pattern

The decentralized pattern is better suited to the more familiar support functions that do not require complex training, supervision, and evaluation. It is the most economical of the three patterns because it does not create another supervisory position. However, it cannot provide for specialists' training, and it is relatively inflexible because the individuals cannot easily be shifted around to handle peak loads.

The structurally organized but physically scattered group of specialists provides a means of administering the higher grades of professional skills; solves many personnel problems by its own internal flexibility; and handles seasonal peaks by the external flexibility that enables it to keep pace with the waves of work through the organization. It aids morale by providing a means of treating professionals like professionals, in terms of control, evaluation, and supervision. It requires more experience, diligence, and competence in its supervisor than the centralized group does because he must move about to do his work, have considerable insight into the work problems of the specialists, and coordinate his effort with many different supervisors. This pattern might cost more than the other two, but it usually repays the extra cost in better service and support. ♦

ALSO RECOMMENDED



summaries of other timely articles

GENERAL

MAKE JOBS PAY THEIR WAY. By Joseph G. Mason. *Nation's Business* (1615 H Street N. W., Washington 6, D.C.), September, 1961. Reprints 10 cents. Cutting manufacturing costs and increasing productivity are only part of the cost-cutting process; management must also seek more performance and less waste in the management function itself, the author states. He proposes adapting the value-analysis approach to examine five areas of business: actual administrative functions; the time spent in carrying out administrative details; the manpower used in each function; the facilities available for the administrative job; and outside services rented or purchased. In his discussion of each section, the author provides sample questions to guide the reader's analysis.

CORPORATE HORIZONS. By Edmund K. Faltermayer. *The Wall Street Journal* (44 Broad Street, New York 4, N.Y.), October 25, 1961. 10 cents. General Electric Co. is forecasting consumer buying patterns for 1980; U.S. Steel Corp. is currently estimating how much iron ore it will need in the year 2000; General Mills, Inc., is now predicting the percentages of gross investment, sales, and profits it will have in entirely new products it will develop between now and 1966. These and other examples of long-range planning described by the author are only a few in an increasingly common effort among U.S. corporations to look ahead and to place in one document hoped-for growth rates and the principal actions that will be necessary to achieve them.

IS EXECUTIVE COMPENSATION IN LINE IN YOUR COMPANY? By Charles F. Johnson. *Business Management* (22 West Putnam Avenue, Greenwich, Conn.), October, 1961. 75 cents. One chart in this article—which is based on a year-long survey of executive compensation—details the median compensation for fifteen common management positions in three different annual-gross categories; another compares the chief executive's compensation with that of the second- and third-ranking executives in 325 publicly owned corporations; and others depict the compensation of dual-role executives, the decline of executive take-home pay, and exactly what a thousand-dollar-per-year raise means to the executive. The author also offers several general observations on current executive-compensation trends.

HELP FROM THE COMPANY ECONOMIST. By Henry B. Arthur. *Harvard Business Review* (Soldiers Field, Boston 63, Mass.), September-October, 1961.

Please order directly from publishers

Reprints $1.00. The who, how, why, and what of the man who performs an invaluable service in corporate decision-making—the translation of highly technical economic techniques into practical business terms. For the executive bewildered by higher mathematics involved in econometrics, linear programing, and simulation, the author explains the role of a company economist in solving these problems as well as his part in broader aspects of planning such as forecasting, policy formation, measurement of potential, and public relations. He cites instances that show how company economists have helped shape major policy decisions in large corporations.

PRODUCTION

COMING ERA IN ENGINEERING MANAGEMENT. By Clinton J. Chamberlain. *Harvard Business Review* (Soldiers Field, Boston 63, Mass.), September-October, 1961. Reprints $1.00. The trend toward one-of-a-kind or few-of-a-kind production and the greatly increased technical content of many products pose serious problems for engineering management, because although the number of engineered products is decreasing, their increase in size and complexity requires much greater engineering effort. This increased demand on the individual engineer's capability calls for better planning, organization, staffing, and control from the engineering manager, who already faces stiff competition for the services of superior engineer-scientists. For companies that depend on scientific and engineering development, the author suggests and explains "systems engineering"—the discipline of utilizing the resources of an organized team for the solution of an engineering problem.

SOLID STATE IN CONTROL. *Control Engineering* (330 West 42 Street, New York 36, N.Y.), September, 1961. $2.00. Solid-state devices and systems offer performance characteristics and capabilities that cannot be duplicated in any other way, notes *Control Engineering*, as it offers a special issue devoted to this significant development. Seventeen articles by authorities in the solid-state field are grouped under seven major headings: basic engineering concepts, measurement, data transmission, decision-making and storage, power modulation and generation, information display, and molecular electronics. While several of the articles describe laboratory-stage research in the field, others illustrate how an engineer can apply solid-state techniques and equipment to today's control problems.

TRAVEL CHARTS POINT OUT MH BENEFITS. By W. A. Lynam. *Material Handling Engineering* (812 Huron Road, Cleveland 15, O.), September, 1961. 75 cents. Laying out a new plant? Trying to improve an old one? If so, the author suggests, travel charts can help you reduce materials handling and give you a quantitative index of the benefits of each of several possible layouts. The materials-handling travel chart, as developed by the author, resembles a mileage chart on a map; he describes how to use it in simple and complex situations, how to develop a chart from data, and how to analyze the information it offers. Tables illustrate how the system—combined with mathematical analysis and common sense—can improve materials-handling layout.

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FOREIGN OPERATIONS

STAFFING ROUND-THE-WORLD JOBS. *Business Week* (330 West 42 Street, New York 36, N.Y.), October 7, 1961. 50 cents. Foster-Wheeler Corporation, an engineering company that carries on 50 per cent of its business abroad, has found that the best man for a foreign operation is not necessarily the man who speaks the language or understands the customs well, but the man with high-level engineering or supervisory capabilities. The men who are sent abroad face all the routine problems involved in building large industrial plants, as well as complications arising from being in a strange country: scarcity of labor, extremes in climate, lack of recreation facilities, and difficult living conditions. Nevertheless, the man who knows his job seems to thrive, and most of the men originally selected continue in various expatriate assignments.

WEST GERMANY. *Steel* (Penton Building, Cleveland 13, O.), October 16, 1961. Reprints gratis. West Germany's imports of finished goods increased 25 per cent from 1959 to 1960 and accounted for 32 per cent of total imports (the average for the 1954-58 period was about 19 per cent). This means that West Germany is becoming an even more important market for U.S. producers of capital equipment, consumer durable goods, and some types of materials, according to this article, which points out areas of untapped market potential in the West German market. The article includes a rundown of West German production in various industries and details on economic conditions, as well as information on population, currency, government, and the like.

PICK A PRO FOR OVERSEAS. By Jack J. Friedman. *Dun's Review and Modern Industry* (99 Church Street, New York 8, N.Y.), October, 1961. 75 cents. How do you pick the man for a touchy overseas job? The author reports on how three oil giants, with decades of experience in lands around the globe, do it. Based on their descriptions, the man to send abroad has these characteristics: (1) He will want to go abroad; (2) he will have what the oilmen call "an international outlook," never an easy matter to determine; (3) he will be young, probably married; and (4) he will speak the language of the land to which he is going or have an aptitude for learning it.

MARKETING

WHAT ELECTRONIC COMPUTERS CAN DO IN SALES FORECASTING. By Gerhard Bry. *Sales Management* (630 Third Avenue, New York 17, N.Y.), September 15, 1961. 50 cents. The electronic computer revolution, which has changed many factory and office procedures in radical ways, has also affected sales forecasting, although the impact has admittedly not been great so far, according to this semitechnical discussion of the current and prospective uses of electronic computers in forecasting. The author makes a distinction between general economic forecasting, market-demand forecasting, and company-sales forecasting, since these fields are differently affected by the computer

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technology. He also discusses short-term and long-term forecasting separately, since they differ in basic data, statistical approaches, and computational requirements.

CLUES FOR ADVERTISING STRATEGISTS. By Donald F. Cox. *Harvard Business Review* (Soldiers Field, Boston 63, Mass.), September-October, 1961. Reprints $1.00. Basic assumptions about mass communications prompt advertisers to use a particular message for a specific audience, but the author points out that these assumptions are not necessarily in accord with recent findings of research in advertising and mass communications—findings that may have valuable implications for advertisers. The topics examined and reported upon include degree of credibility of the communicator; influence of "emotional" vs. "rational" appeals; effectiveness of a one-sided or two-sided argument; and the value of repetition of a message.

PRODUCT MAKERS GET EARFUL FROM WOMEN. *Business Week* (330 West 42 Street, New York 36, N.Y.), October 14, 1961. 50 cents. A drinking fountain in the garage? An all-appliance kitchen? Marketers and manufacturers heard these ideas and others at the Fifth Annual Congress on Better Living sponsored by *McCall's Magazine*, where 66 women discussed a variety of subjects—appliances, cars, toothpaste, houses, travel, education, health, charge accounts, supermarkets, drugs, and table settings. The discussions brought out several patterns and clues to the market. Among those of particular interest: (1) In what appears as an amazingly diverse market there is ample room for change and innovation; homemakers are eager to hear new ideas; (2) a strong streak of practicality is shown by concern for length of service and resale value of major purchases; (3) family health and safety are primary factors in shaping buying habits.

OFFICE

HOW MUCH SPACE . . . AND WHERE? and **SAMPLE OFFICE LAYOUTS.** By J. J. Murphy. *Office Executive* (1927 Old York Road, Willow Grove, Pa.), October, 1961. 50 cents. Determining how much space an office needs is 50 per cent simple arithmetic (a given number of pieces of office furniture occupy a certain number of square feet) while the remaining 50 per cent is a matter of judgment, the author declares. In his first article, the author offers many facts and figures an administrator should know in order to efficiently plan the layout of an office; in his second article, he presents three detailed drawings of sample office layouts.

PLANNING FILES FOR A SKYSCRAPER OFFICE. By Thomas Wilds. *The Office* (232 Madison Avenue, New York 16, N. Y.), September, 1961. A step-by-step explanation of how one company completely revamped its file equipment when it moved into a fifty-story skyscraper from fourteen scattered Manhattan locations. Before the move, the company had 5170 files occupying 30,292 square feet; after the move, it had 3200 units occupying 19,200 square feet—a saving of 11,000 square feet, or roughly the equivalent of one tower floor. Since the skyscraper is a modular building where walls are movable, all the space saved can be used.

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SURVEY OF BOOKS

for executives

The Six and the Seven

EUROPE AT SIXES AND SEVENS: The Common Market, the Free Trade Association, and the United States. By Emile Benoit. Columbia University Press, 2960 Broadway, New York 27, N.Y., 1961. 275 pages. $5.00.

*Reviewed by J. Wilner Sundelson**

This interesting book provides information on three distinct but related problems. First it describes the European Common Market's background, structure, and early functioning, the United Kingdom's abortive attempt to sell its ideas about a free-trade zone, and the European Free Trade Association. The treatment of this topic includes an attempt to look at the EEC in the broad setting of the combat for survival between the Western world and the Soviet bloc and to delineate the role of the EEC in the tasks lying ahead—forging the Atlantic community and aiding the underdeveloped nations.

The second main subject is the problem of the United States' balance of payments, with particular emphasis on the cost competitiveness of American products in world markets. In analyzing this question, the book tries to deal quantitatively with the probable impact of the EEC tariffs on American exports.

The final subject discussed is the economic growth potential of the EEC and the desirability of some form of American participation. There is also a brief rundown of the general climate for American investments in the various countries of Europe.

Among the more interesting highlights of the book is its support of EEC's claim that it is not protectionist in aim. Professor Benoit asserts that the common tariff wall would have been higher than it is if any effort had been made to take account

* Regional Group—European Operations, Ford International Staff, Ford Motor Company.

of the volume of each product traded. This means that the average producer within the tariff area will enjoy a lower level of protection at the end of the EEC tariff drill than he did before. Another point brought out is that the EEC has done very little, if anything, in the major spheres of economic integration other than its internal trade liberalization and common external tariff. Nothing has been accomplished in the direction of freeing the movement of capital and labor, and virtually nothing has been done in connection with agriculture or transport.

In retrospect, it now seems that Professor Benoit has placed too much emphasis on the United Kingdom's difficulties in joining the EEC and too little on the role played by political determination. The history of the EEC itself shows clearly that no basic steps in European integration have been taken without strong political determination, which has in each case preceded the efforts of experts and technicians.

After giving a good résumé of developments in the United States' balance of payments since World War II, the author attempts to summarize the evidence in support of the view that there has been a real decline in our price competitiveness. Though our rate of wage increases has not been higher than that of Europe, he points out, there has been a definite slowness in our rate of productivity advance, and wage costs per unit of output have risen faster here than in Europe. Understandably, the book offers no solution for this grave national problem.

Professor Benoit agrees with those who estimate that only some 5 to 10 per cent of our traditional exports to Europe are likely to be materially affected by the EEC's tariff discrimination. He does make the point, though with insufficient emphasis, in this reviewer's opinion, that the thing to look at is the fast growth rate anticipated for an integrated Europe—an economic phenomenon that will have a much greater impact on America's export potential than any tariff reshuffling.

His discussion of the opportunities facing U.S. business lays perhaps too much stress on community-wide trade possibilities for a manufacturing or assembling activity within the EEC. For some time to come—in fact, for a virtually indefinite period, in the case of a great number of products—investors going into the EEC will have to conform to the business climate in a particular country and will have to compete with companies trying to sell enough in that country to achieve the reputation and economies in costs that will eventually enable them to export. EEC today is still an association of independent national economies engaged in the construction of a customs union.

Professor Benoit also presents the case for U.S. investors' taking partners, or at least minority shareholders, abroad. Much of his argument on this question seems to be more relevant to underdeveloped countries than to the advanced economies of the EEC countries. Also, he fails to make any case at all for 100 per cent ownership, which is common and quite acceptable in Western Europe, particularly for basic manufacturing facilities.

For the reader who did not keep up with integration movements in Europe before the U.K. and some of its associates in EFTA decided to seek membership in EEC, or some other form of association with it, *Europe at Sixes and Sevens* is probably the best available introduction with a strictly American focus. A great many interesting facts, with a minimum of errors, are packed into a worthwhile contribution that sheds considerable light on the American economy and the kind of competitive trading world it now has to live with. ♦

Formula for Human Relations

THE ART AND SKILL OF GETTING ALONG WITH PEOPLE. By Sylvanus M. Duvall. Prentice-Hall, Inc., Englewood Cliffs, N.J., 1961. 246 pages. $4.95.

*Reviewed by Robert F. Pearse**

The aim of this book is to develop a simple, concise outline of the principles of human relations. The author has tried to avoid the traps into which so many do-it-yourself books on handling people have fallen—overgeneralizing and oversimplifying. How well he has succeeded depends on the individual reader's orientation and expectations.

Those well grounded in theory and research in interpersonal relations will probably find his formula-centered approach too vague and general to be of much use in coping with the complexities of actual human relations. Those looking for a quick set of magical rules for getting what they want out of others will be so busy trying to memorize Dr. Duvall's formulas that they will ignore the philosophy and psychology he has attempted to put behind them. A third set of readers, however—those who want to gain practical insight into themselves and others without undergoing training in clinical psychology—may find this book interesting and helpful.

Dr. Duvall suggests that an important key to improving our relations with other people lies in knowing what to expect from them. He advises us to be realistic in selling what we have to offer, seeking out those who need it and can also afford it and not wasting time trying to change the unchangeable in human nature.

A section on self-concepts and needs is followed by one on how to size up people "from the inside" and "from the outside" on the basis of their behavior. Other sections deal with whom to trust (and why) and techniques for influencing others. The strategies advocated in this last section are not new, however, and have been touched on by other writers concerned with the development of human-relations skills.

In considering the value of books of this kind, the question always

* Director of Personnel, Stop & Shop, Inc.

arises, "Can people really improve their human-relations skills simply by reading a how-to book on the subject?"

There is no doubt that some degree of conscious improvement in human relations can be attained through reading a clear and concise book such as Dr. Duvall's, just as it is possible to learn the fundamentals of dancing or cooking through reading alone. But the trouble with merely reading about human-relations skills is that in applying what we have read we tend to modify it in accordance with our own prior attitudes and perceptions. This automatically limits our capacity for more effective human relations.

With this basic limitation kept in mind, it can still be said, however, that Dr. Duvall's book is better than many of the superficial treatments of the subject that have appeared in recent years. ♦

Briefer Book Notes

(Please order books directly from publishers)

GENERAL

THE PROMISE OF ECONOMIC GROWTH: *Prospects, Costs, Conditions*. (Report of the Committee on Economic Policy.) Chamber of Commerce of the United States, Washington 6, D. C., 1960. 56 pages. Single copies, $1.00. Maintaining that economic growth has become a political as well as an economic issue, this report sets the problem in its context and provides a foundation for intelligent discussion and decision. Among the topics considered are the several meanings of growth; the content of growth in goods, services, and leisure; higher structural unemployment; and the obstacles to growth.

ECONOMICS AND AMERICAN INDUSTRY. By Leonard W. Weiss. John Wiley & Sons, Inc., 440 Park Avenue, New York 16, N.Y., 1961. 548 pages. $7.50. Examining the actual performance of the seven industrial organizations that participated in this survey, the author discusses and evaluates significant concepts of economic policy. He goes on to describe the organizational structure of each industry represented; its performance in terms of output capacity, prices, and profits; and public policy toward business.

1961 PLANT LOCATION. Simmons-Boardman Publishing Corporation, 30 Church Street, New York 7, N.Y., 1961. 332 pages. $15.00; educational institutions and libraries, $10.00. This edition provides the latest figures on all important factors affecting plant location, including the final counts of

the 1960 Census. Among other features are an enlarged state-by-state labor and manufacturing section, improved state maps, and better indexing for quick reference.

SOLVING FOREIGN BUSINESS PROBLEMS: *Case Studies of 100 Companies*. Business International, 200 Park Avenue, New York 3, N.Y., 1961. 130 pages. $30.00. This collection of actual case histories shows how over 100 leading companies overcame a variety of problems in earning overseas profits. Each case suggests practical new ideas that are applicable to many of the challenges confronting companies of every size operating abroad. Among the problems discussed are organizing for maximum flexibility and profit in international operations, specific difficulties in finding capital for expansion abroad, selling the growing African market, and deferring U.S. taxation on foreign income to accumulate maximum capital for overseas investment.

GRAPHICAL ECONOMICS. By J. L. Eastham. Quadrangle Books, Inc., 119 West Lake Street, Chicago, 1, Ill., 1961. 334 pages. $6.00. A graphical treatment of such economic concepts as demand and supply; input-output relationships; wages; the theory of rent; money, interest, and price level; and income and employment. Designed for the practicing manager as well as for the student.

PAPERWORK MANAGEMENT: *A Manual of Workload Reduction Techniques*. By H. John Ross. Office Research Institute, P.O. Box 744, Miami 43, Fla., 1961. 348 pages. $20.00. A guide for the manager responsible for reducing and controlling the flow of paperwork in his company. Provides a number of actual records and documents, illustrating the types of controls discussed.

TRADE DIVERSION IN WESTERN EUROPE. (Occasional Paper No. 9.) Political and Economic Planning, 16 Queen Anne's Gate, London, S.W. 1, Eng., 1960. 50 pages. 5 shillings. In discussing the pattern of trade of the EEC and EFTA countries both with each other and with the rest of the world, this paper attempts to identify the probable diversionary impact on that trade of the tariff changes called for by the Treaties of Rome and Stockholm.

MARKETING

PROCEEDINGS OF THE 17th ANNUAL ADVERTISING AND PROMOTION EXECUTIVE CONFERENCE: *October 21, 1960*. The Bureau of Business Research, Ohio State University Publications, The Ohio State University, Columbus 10, Ohio, 1961. 96 pages. Gratis. Papers from this conference include discussions on mobility and sales ability, fresh ideas for successful advertising, and advertising opportunities in films.

GUIDEPOSTS FOR DECISION MAKERS. Super Market Institute, Inc., 500 North Dearborn Street, Chicago 10, Ill., 1961. 80 pages. $5.00. The proceedings of a conference held at Bal Harbour, Florida, under the sponsorship of the Super Market Institute. Among the problems considered are more effective store management, guideposts to performance, and new competition.

DIRECT MAIL SHOWMANSHIP. By Dick Hodgson. American Marketing Services, Inc., 610 Newbury Street, Boston 15, Mass., 1961. 136 pages. $17.50. A detailed discussion of "showmanship" techniques for all types of direct-mail advertising, illustrated with over 100 actual case histories. Includes a 20-point checklist for analyzing the showmanship potential of any direct-mail piece or package.

SELECTED CASES IN MARKETING MANAGEMENT. By David E. Faville. Prentice-Hall, Inc., Englewood Cliffs, N.J., 1961. 352 pages. $6.60. A collection of actual case histories emphasizing the managerial approach to marketing. Focusing on decision-making and the strategy the marketing manager needs to adapt his marketing mix to rapidly changing conditions, the author deals with such subjects as depth interviews, creating a brand image, self-service, determining coverage for a new industrial product, and testing advertising copy appeal.

MARKETING RESEARCH. (Second Edition.) By David J. Luck *et al.* Prentice-Hall, Inc., Englewood Cliffs, N. J., 1961. 542 pages. $11.35. This completely revised and updated text covers such recent developments in the field as motivation research and operations research. New cases and problems have been added, while much of the technical material has been simplified.

GUIDELIST FOR MARKETING RESEARCH AND ECONOMIC FORECASTING. (AMA Research Study No. 50.) By Robert N. Carpenter. American Management Association, 1961. 96 pages. AMA members, $2.50; nonmembers, $3.75. An attempt to provide a broad outline of available publications and other sources of facts pertinent to the marketing field. Comprehensive bibliographies and directories include topics that, though they may not necessarily appear in this report, nevertheless offer the researcher leads to additional, more specialized reports.

SALESMANSHIP: *Helping Prospects Buy*. (Third Edition.) By C. A. Kirkpatrick. South-Western Publishing Company, Inc., 5101 Madison Road, Cincinnati 27, Ohio, 1961. 532 pages. $6.50. In this edition, many sections have been rewritten, while several chapters have been shortened or expanded. Includes a new chapter on industrial selling as well as new examples, study assignments, and case studies.

MANAGEMENT REVIEW

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Q&A on AMA

Q. *There seem to be publications and meeting announcements from several AMA Divisions which are not being received by any of our firm's enrolled members. Can our membership be expanded to incorporate these additional areas?*

A. The Association is currently issuing publications and sponsoring meetings in eleven Divisions: General Management, Personnel, Finance, Manufacturing, Research and Development, Packaging, Marketing, Insurance, Administrative Services, International Management, and the newest Division, Purchasing. Your company's AMA membership enrollments should be reviewed if new key employees have joined your staff, if the corporation has become more deeply involved in particular subject areas, or if new AMA Divisions have been established since the last general review.

The Membership Department at AMA headquarters will provide information and assistance in revising and expanding the coverage of any membership.

✱ If you have any questions about AMA's program or policies, please submit them to AMA's Member Relations Department. All inquiries will be answered promptly. Those questions of most general interest will appear in this feature in subsequent issues of *Management Review*.